

PRINCIPLES OF MERCANTILE LAW

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PRINCIPLES OF MERCANTILE LAW

CHAPTER I

SOURCES OF MERCANTILE LAW

“Law Merchant”

The term “Law Merchant” or “*Lex mercatoria*”, as understood in English Law, signifies a body of legal principles founded on the custom of merchants in their dealings with each other. It was at first distinct from the Common Law but afterwards became incorporated with it. A separate name is given to this branch of the law because it applies to particular subjects, principles more or less different from those which the Common Law recognises in other matters and also because these principles were engrafted upon English Law by a process of gradual adoption, from the general body of European Usages in matters relating to commerce (a). These usages being proved before the Courts of Law, have been adopted by them as settled law, on the well-known principle that with reference to transactions in different departments of trade, Courts of Law, in giving effect to the contracts and dealings of the parties, will affirm that the latter have dealt with one another on the footing of some custom or usage prevailing in that department. Thus the “law merchant” is neither more or less, than the usages of merchants and traders in the different departments of trade, ratified by the decisions of Courts of Law. What before was usage only, unsanctioned by legal decision, has become engrafted upon or incorporated with the Common Law (b).

The special feature of Mercantile Law of England noted above, viz. that it is mostly the result of custom and is generally uncodified, is not peculiar to this particular branch of English Law only. In fact, by far the largest portion of English Law is unwritten and uncodified, and is generally to be gathered from legal treatises of eminent jurists and the decisions of Courts of Law. Thus English Common Law is a body of principles evolved by judicial decisions based on the general custom of the realm. Equity again is another body of legal principles enunciated by the Lord Chancellors of England in deciding questions of disputed rights coming before them for their decision. Acts of Parliament undoubtedly form one of the sources of English Law but the range of subjects covered by them is comparatively restricted and they have acquired such importance as they possess, only in very modern times.

Sources of Mercantile Law in India

As distinguished from its English counterpart, the Mercantile Law of India does not derive its foundation from the prevailing custom of merchants but is based on various enactments of the Indian Legislature which have codified the principles of law applicable to mercantile transactions. Thus the law as regards commercial contracts is to be found in the “Indian Contract Act”. The law as regards Bills of Exchange and Cheques is laid down by the “Negotiable Instruments Act”. The Law of Sale of Goods,

(a) *Encyclopædia of Laws of England.*

(b) *Goodwin v. Roberts* (1875), L.R. 10. Ex. 337.

of Partnership and of Incorporated Companies is laid down in the "Indian Sale of Goods Act" of 1930, the "Indian Partnership Act" of 1932 and the "Companies Act" of 1956 respectively. These and other Indian Legislative enactments dealing with Mercantile Law are undoubtedly based on and attempt to embody in themselves the corresponding principles of English Law applicable to the respective topics. The principles, however, having been reduced to the form of enactments, it is no longer permissible to go beyond or behind their enacted provisions or to refer to the corresponding provisions of English Law on the respective subjects. Indian Mercantile Law may thus be said to be a creature of Statutes. In saying this, however, one must not lose sight of the fact that where a legal enactment does not specifically provide for a particular point or where there is no specific legal enactment covering a particular branch of law, the principles of English Law applicable to such cases and subjects are still to be followed (c). Thus the Indian Contract Act makes no provision for contract of carriage and affreightment; the principles of English Law relating to these subjects have therefore been followed. Similarly, there is no Act of the Indian Legislature dealing with maritime transactions between merchants. In its absence, therefore, the Law Maritime as administered by the Admiralty Courts in England is followed in India.

This however does not mean that custom as a source of mercantile law is not recognised by Indian Jurisprudence. Many Indian Statutes make specific provision to the effect that the rules of law as laid down in a particular Act are subject to any special custom or usage of trade, which is not inconsistent with its provisions. Thus the Indian Contract Act provides that nothing therein contained "shall affect any usage or custom of trade" (sec. 1). In the same way, the Negotiable Instruments Act provides that nothing therein contained "shall affect any local usage relating to any instrument in an oriental language" (sec. 1). Apart from such special statutory provisions, it may be mentioned that the whole law relating to Hundis and the Kachi and Pakki Adat systems of agency is based on custom and usage of trade as recognised and given statutory effect to, by Courts of Law in India.

"Mercantile Custom"—nature of

"Mercantile custom" as the term is here used, is different from local custom and "customary law" as applicable to the different communities in India under various Letters Patent and other legislative enactments. As was pointed out by their Lordships of the Privy Council in *Jaggomohan Ghose v. Manekchand*, 7 Moo I.A. 263, to support a mercantile custom there need not be either antiquity, uniformity or notoriety. "The usage may still be in the process of growth, it may require evidence in each case, but in the result, it is enough if it appears to be so well known and acquiesced in, that it may be reasonably presumed to have been an ingredient imported by the parties into their contract." The Bombay High Court has laid down that in order to prove a usage in a particular trade, it must be shown that the usage is (i) certain, (ii) reasonable, (iii) not inconsistent with law, and (iv) so universally acquiesced in, that everybody engaged in the trade knows it or could ascertain it if he took pains to inquire (d).

(c) *Mayor of Lyons v. E. I. Co.*, 1 M.I.A. 175.

(d) *Jamnadas v. Chetandas*, 30 Bom. L.R. 1317.

CHAPTER II

LAW OF CONTRACT

The Contract Act—its application (sec. 1)

The "Indian Contract Act" was enacted by the Indian Legislature in 1872. It came into force on the 1st of September of that year. It applies to the whole of India, except the State of Jammu and Kashmir. The Act is not retrospective. It is also not exhaustive. The Act attempts to lay down certain principles of law governing contracts. Other Acts of the Indian Legislature also contain provisions of law as regards contracts, e.g. the "Negotiable Instruments Act" which deals with the law as regards contracts represented by negotiable instruments, the "Transfer of Property Act" which deals with contracts relating to immovable property, the "Specific Relief Act" which deals with the law as regards specific performance of contracts, the "Registration Act" which deals with questions of registration; the "Limitation Act" which, among other things, deals with the law as regards limitation of suits relating to contracts, the "Evidence Act" which, among other things, deals with the law as regards the proof of contracts, the "Usurious Loans Act", "Merchant Shipping Act", and many others. This is also clear from the preamble to the Act which says that the purpose of the Act is "to define and amend certain parts of the law relating to contracts". Thus it has been held that the special rule of Hindu Law, viz. of "Damdupat", which lays down that no Hindu creditor can recover from his Hindu debtor, at one time, more than double the amount for principal and interest is not affected by the Contract Act (c). The rule of Damdupat is operative in the whole of the Bombay Presidency and in the town of Calcutta but not elsewhere.

As sec. 1 further lays down, the Act does not affect the provisions of any Statute, Act or Regulation not expressly repealed thereby, nor any custom or usage of trade nor any incident of any contract not inconsistent with the provisions of the Act. Thus the provisions of the Act are not to modify (i) any of the special provisions of any other unrepealed enactment; (ii) any particular usage or custom of trade which may govern a contract appertaining to that particular trade, e.g. custom of arbitration, custom as regards "kachi" and "pakki Adat", etc.; (iii) any particular term of a contract which the parties have mutually agreed to, though it differs from the rule laid down in the Act in that behalf. Thus though the Act gives a right to a party against whom a contract is broken, to sue for damages for all loss caused to him by the breach, the Act does not make illegal a provision in a contract that on breach, only nominal damages should be recoverable. The only qualification is that such special term must not be "inconsistent with the provisions of the Act". Thus a provision in a contract that the contract shall not be voidable on the ground of fraud would be bad. Notice that a custom, inconsistent with the terms of a contract, cannot be set up (f).

Scheme of the Act: The Act is divisible into two parts. The first part (secs. 1-76) deals with the general principles of the law of contracts and therefore applies to all contracts irrespective of their nature. The second part (from secs. 76-238) deals with certain special kinds of contracts, e.g. of

(c) *Harilal v. Nagar* (1896), 21 Bom. 38.

(f) *Ruttonsi v. Bombay United Co.*, 18 Bom. L.R. 532.

guarantee and indemnity, of bailment and pledge, agency, etc. Before 1930 the Act contained provisions relating to contracts for sale of goods as well as partnerships. As these provisions failed to cover various important questions arising with reference to the above types of contracts, the Indian Legislature in 1930, abrogated the portion of the Act dealing with sale of goods (secs. 76-123) and enacted a new Act called the "Sale of Goods Act" embodying an up-to-date, concise and clear exposition of the law applicable to sale of goods (see seq.). Similarly in 1932, the Indian Partnership Act was passed, after repealing the corresponding provisions in the Act relating to partnerships (secs. 239-266) (see seq.).

How a contract is made (sec. 2)

Sec. 2 of the Act apparently gives a series of definitions of terms which are used subsequently in the body of the Act. The sec. however is also important because it attempts, by a side-door, to describe how a contract comes into being. Several steps are involved in the making of a contract. There must be (i) a "proposal" and (ii) an "acceptance" of the "proposal". (iii) A proposal when "accepted" becomes a "promise" cl. (b). (iv) Every "promise" (and every set of "promises" forming consideration for each other) amounts to an "agreement". (v) All "agreements", however, are not "contracts". (vi) A "contract" is an "agreement" "enforceable by law" cl. (h). (vii) What is essential in order to turn an "agreement" into a "contract" is, among other things, "consideration" cl. (d). In thus laying down analytically the various steps which the making of a contract involves, the framers of the Act have, to a great extent, simplified, what in text books on English Law, forms, on the whole, a very complicated and a somewhat abstract subject. Having thus conveyed to the student the process of the formation of a contract in outline, the Act in the same sec. proceeds to define and explain the various terms used above.

Definitions (sec. 2) Proposal: "When a person signifies to another, his willingness to do or abstain from doing something with a view to obtaining the assent of the other to such act or abstinence, he is said to make a proposal" cl. (a). The definition involves the following important points: (i) It must be an expression of willingness to do or abstain from doing something (ii) to another person (iii) with a view to obtain his assent thereto, to which may be added a further term, viz. (iv) that the expression of willingness must be made with a view to create legal obligations (Anson).

Thus there can be no "proposal" by a person to himself. It must always be to another person. Further, it must be made with a view to obtain the assent of the other. Thus a casual inquiry or a mere statement of intention is not a proposal. As an instance illustrating (iv), may be mentioned an invitation for dinner, which, though accepted, will not become an "enforceable agreement," i.e. a "contract", because, though it fulfils all the other conditions of a "proposal", it does not satisfy the last condition, as it is not made with the intention of creating a legal liability. Similarly, where parties expressly stipulate that the agreement will not be legally enforceable but shall only bind the parties as a matter of honour, no contract will arise (g).

Whether in given circumstances, there has been a "proposal" is a question of construction depending upon the facts of each case. A "proposal" is also sometimes called an "offer". An "offer" can be made either orally or in writing or by conduct. In the first two cases it is said to be "express". In the last case it is called "implied".

A tramway company running trams on a particular route makes an "implied" offer to carry intending passengers over the route at the scheduled price. A receipt is not an "offer" so as to bind the acceptor to the terms thereof. Thus where A hired a deck chair from a Council and having paid the hire, was given a ticket, which contained a clause exempting the Council from liability for accidents and damages, it was held that the acceptance of the ticket did not prevent A from suing the Council for injury caused to him by his chair collapsing (h).

Invitation for an offer: An "offer" must be distinguished from what is, in substance, and in fact, an invitation to treat or as it sometimes called, an "invitation for an offer". In the latter class of cases there is no intention on the part of the person sending out the invitation, to obtain the assent of the other person to such "invitation". His object is merely to circulate information of his willingness to treat with anybody, who, on such information, is willing to open negotiations with him. Such "invitations for an offer" are, therefore, not "offers" and do not become "promises" by their "acceptance".

Thus a bookseller's catalogue is not an "offer" which by acceptance becomes a binding contract obliging the bookseller to sell a book at the advertised price but merely an "invitation for an offer". Similarly, a railway company's time-table is an "invitation for an offer" and not an offer to run trains at the scheduled time (i). Similarly in India a quotation of terms of business by a commission agent to an upcountry constituent has been held to be merely an "invitation for a proposal" (and not a "proposal"), which becomes a binding agreement only when the customer places an order on those terms, and the same is accepted by the merchant (j). An "offer" must also be distinguished from a "declaration of intention". Thus where an auctioneer advertises a sale on a particular day, he is not liable in damages, on his subsequent cancellation of the sale, to any person who, on the faith of the advertisement, has incurred expenses for attending the proposed sale (k). In a recent English case, a chemist running a "self service" shop had placed certain medicinal preparations on an "Island" fixture in his shop with prices marked on each article. A customer having picked up some of these, went to the cashier, who totalled the price and accepted payment. Held, the taking of the article from the shelves on the "island" constituted an "offer" by the customer to buy and not an acceptance by him of the chemist's "offer" of sale (l).

Standing Offers: Sometimes a "proposal" may take the form of a continuous offer. Such offers are called "standing offers", though sometimes they are also popularly called "promises". Thus a "promise" by a banker to discount a person's bills upto a certain limit, a "promise" by a dealer to supply goods to another for a fixed period at particular prices, are not really "promises" (i.e. accepted offers) but merely a series of continuous offers made by the party in question, which only become binding "promises" when the party to whom they are made accepts the same by drawing a bill or placing an order, as the case may be, in accordance with the terms of such offers. Thus where A "agreed" with B to sell him certain lands on the payment of the price before a particular day in any future year, at the option of B, it was held that this was not an "agreement" at all, but a standing offer on the part of A, which would become a binding contract only when B exercised the option (m). A public offer of a reward for doing something, is another instance of a "standing offer".

Tenders: Transactions which result from what are popularly called "tenders" may also be mentioned here. In general a "tender" is an offer

(h) *Chappleton v. Barry* U. D. C. (1940), 1 K.B. 532.

(i) *Grainger v. Gough* (1896), A.C. 325.

(j) *Malappa v. Aga Mirza*, 37 Mad. L.J. 712.

(k) *Harris v. Nickerson* (1873), L.R. 8

Q.B. 286.

(l) *Pharmaceutical Society of G. B. v. Boots Cash Chemists* (1952), 2 All E.R. 456.

(m) *Papa Naidu v. Muniswami*, 46 Mad. 30.

to supply goods on the terms submitted, when an order is placed in accordance with those terms by the other party. From this viewpoint, a "tender" is merely a "standing offer" which does not become a "contract" on the tender being "accepted" but becomes a binding agreement only when an order in terms of the tender is placed by the other party with the tenderer. The result is that till such an order is placed, both parties are free from all legal obligations with regard to the "tender". The party "accepting the tender" is not bound to place any order with the tenderer in terms of the tender; nor is the tenderer bound to abide by the terms of the "tender", which he can always withdraw before the other party has "accepted" the terms by placing an order with the tenderer according to them (n).

It should be noticed, however, that "tenders" may take other forms. They may amount to a contract of purchase and sale. Thus where Government invites tenders for the supply of a certain quantity of cloth of a particular kind, i.e. 10,000 yards of tentage and X's tender for the same is accepted, a contract of sale and purchase has come into existence. A "tender" may also be for the supply of an unspecified quantity of goods, e.g. a tender for the supply of the "usual requirements" of a particular department. On such a tender being "accepted", the acceptor does not become bound in law to take any specified quantity of the goods in question from the tenderer but he would be guilty of a breach of contract if, requiring the goods, he purchase them from a person other than the tenderer (o).

Acceptance: When the person to whom the proposal is made signifies his assent thereto it is said to be "accepted" [cl. (b)]. Whether an "offer" has been "accepted" or not, is always a question of fact depending upon the circumstances of each case.

Thus in *Harvey v. Facey* (p) Harvey wrote to Facey: "will you sell Whiteacre? wire lowest price", to which Facey replied: "lowest price £900". Harvey replied: "accepted; send title deeds"; to which Facey sent no reply. *Held*, there was no contract, because Harvey's proposal "to sell" had never been "accepted" by Facey. In a recent Madras case A offered to B (who was an agent for C) to purchase C's bungalow for Rs. 6,000. In reply to B's cable C replied "won't accept less than Rs. 10,000". A accepted the price of Rs. 10,000. C however sold the bungalow to another for a higher price. *Held*, by the Supreme Court, that a mere statement of the lowest price at which the vendor would sell contains no implied contract to sell at that price to the person making the inquiry. Hence C's cable could not be treated as a counter offer capable of resulting in a concluded contract on A's acceptance and that therefore A's suit for specific performance failed (q).

Acceptance depends upon the intention of parties. An insurance company "accepting" the terms of a "proposal" does not thereby enter into an agreement of insurance. Insurance is only effected when a properly stamped policy is issued by the company in return of the premium paid by the assured. Acceptance can either be (i) express, i.e. verbal or written or (ii) implied by conduct, e.g. taking a seat in a tram car is an "acceptance" of the company's "proposal" to run trams on payment of the scheduled fares. The essentials of a valid acceptance are defined by sec. 9 (see seq.).

Promise: "A proposal when accepted becomes a promise" [cl. (b)]. In other words a "promise" is an "accepted proposal". This definition differs from English Law, which regards a promise (i.e. an "offer") under seal as a binding agreement, without the necessity of its formal acceptance by the

(n) *Percival Ltd. v. I.C.C.* (1918), 87 L.J. K.B. 677.

(o) *Keir v. Whitehead* (1938), 1 All E.R. 591.

(p) (1893), A.C. 552.

(q) *MacPherson v. Appanna A.I.R.* (1951) S.C. 184.

other party. Indian Law does not regard a contract under seal as valid, unless it is based on an accepted proposal. Notice that a promise is not equivalent to a "contract". Other ingredients are necessary before a "promise" can, in law, amount to a "contract". These are defined by sec. 10. A "promise" may also be either "express" or "implied".

"Promisor": Promisor means the person who makes the proposal; "promisee" means the person who accepts the proposal [cl. (c)]. In English Law they are respectively called "offeror" and "offeree".

✓ Consideration

"Consideration" is defined by cl. (d) of sec. 2 as follows: "When at the desire of the promisor, the promisee or any other person has done or abstained from doing, does or abstains from doing or promises to do or abstain from doing something, such act, abstinence or promise is called a consideration for the promise." This definition is perhaps the most important of all definitions in the Contract Act, because it defines an ingredient of a contract, which is fundamental for its legal existence. The general rule of law as regards contracts is that an agreement not supported by "consideration" is "*nudum pactum*", i.e. void and of no legal effect. The concept of "consideration" is borrowed by Indian Law from the English Law of contracts. The various elements which go to make up the definition of "consideration" under the Act, are (i) it must be given at the desire of the promisor; (ii) it may be given by the promisee or any other person; (iii) it may consist of an act or abstinence; (iv) it may be either something which happened in the past, or which is done in the present or which is promised in the future; (v) it must be "something" which in the eye of law has a legal value. To put it briefly, "consideration" is something of value which the promisee has given, gives or promises to give in return for the promise. Thus an agreement to sell 100 bales of cotton at a fixed price per bale is a contract, the sellers' promise to sell 100 bales being the consideration for the purchaser's promise to pay the stipulated price therefor and vice versa. On the other hand, a promise by A to B to make a gift of Rs. 1,000 to B is not a contract, as there is no "consideration" proceeding from the promisee B, in respect thereof. The principle on which the doctrine of "consideration" is based is that Law will not enforce or make legally binding, promises which are purely gratuitous. It is only when a promise is made against the receipt of or in return of something of value from the promisee, that such promise will be enforced by law against the person making it. In other words, as Anson puts it, in each case, one must ask the question "does the promisor get any benefit or the promisee sustain any detriment in respect of the promise?" If not, the promise would only be a gratuitous promise, the breach of which may amount to a moral wrong, but which cannot, under any circumstances, amount to a legal wrong which can be redressed by legal remedies in the ordinary Courts of Law.

"Consideration" considered in detail

(1) **At the desire of the promisor**: To take the various ingredients which go to make up the definition of "consideration" in detail, the first essential is (i) that it must be "at the desire of the promisor", i.e. it must be the result of a request proceeding from the promisor. This is a very important feature. "Consideration" given by a promisee voluntarily, without any request from the promisor in that behalf, will not amount to legal consideration so as to support a contract. In a very old Allahabad

promise by B to A to pay for them. In *Sindha v. Abraham* (e), plaintiff rendered services to the defendant during his minority at the defendant's request, which were continued after the defendant ceased to be a minor. After attaining majority, the defendant promised to pay an annuity to the plaintiff for the services. It was held that this was a good contract. Notice that though past consideration is good consideration according to Indian law, it is so only if it is given by the promisee, "at the desire of the promisor". This condition overrides all the other clauses of sec. 2, cl. (d). Consideration may also consist of a present act or abstinence, e.g. a sale of a book on promise to pay the price. It may also consist of a promise to do or abstain from doing something in the future, e.g. an agreement to sell 100 bales of cotton for the January vaida at a specified price, the meaning of which is that the seller promises to sell 100 bales of cotton to the purchaser on the January settlement date, in consideration of the purchaser promising to pay the seller the agreed price on the said date.

(5) **Consideration must be 'something of value':** It is not anything that in law, amounts to "consideration". It must be something which has value in the eye of law. As was said in *Currie v. Missa* (f) "a valuable consideration in the sense of the law may consist in some right, interest, profit or benefit accruing to one party, or some forbearance, detriment, loss or responsibility given, suffered or undertaken by the other". Thus a promise to do that which a person is by law bound to do, does not amount to consideration, e.g. a promise to pay reward in consideration of the other party agreeing to attend Court in pursuance of a subpoena. Similarly, a promise to do something which is manifestly impossible, e.g. to make two straight lines meet or do something which is too vague and unsubstantial, e.g. a promise to pay such remuneration "as shall be deemed right" (g) does not amount to good consideration. Notice that the value of the consideration given need not be equal to the value of the promise. In other words, inadequacy of the consideration will not necessarily make the contract invalid, though it may lead to an inference that the contract was not voluntarily induced.

Executed and executory consideration

Where consideration consists of a present performance, it is called "executed", e.g. present delivery of goods, in consideration of a promise to pay for them, the acceptance of an offer of reward, by supplying the information required. In the first case an act is offered in return for a promise, in the second a promise is offered in return for an act. In cases of executed consideration, one party having already done all he is liable for, leaves an outstanding liability only so far as the other party is concerned. Where and in so far as the consideration consists of promises, it is called "executory", e.g. mutual promises to marry, a promise to build a house in return for a promise to pay according to the architect's certificate. Most business transactions are transactions in which the consideration is "executory".

Agreement : cl. (e)

According to the cl., every "promise" (offer and acceptance) constitutes an "agreement". Similarly, a set of promises forming consideration for each other also amount to an "agreement". Notice that all "agreements" are

(e) 20 Bom. 755.
(f) L.R. 10 Ex. 162.

(g) *Taylor v. Brewer*, 1 M. & S. 290.

not contracts. Certain other elements must also co-exist, before an agreement can, in law, amount to a "contract". What these elements are is stated in sec. 10. An "agreement" may be either (1) "*unilateral*", i.e. in which consideration on one side is executed, e.g. delivery of goods on credit, or (ii) "*bilateral*", i.e. in which consideration is executory on both sides, e.g. mutual promises, called by the Act "reciprocal promises", i.e. "promises forming consideration or part of consideration for each other" cl. (f).

Contract: cl. (h)

A "contract" is defined by the cl. as "an agreement enforceable by law". As to the elements which make an "agreement" "enforceable by law" see secs. 10-30 seq.

Void, voidable and unenforceable

Cls. (g), (i) and (j) of the sec. may be considered together. A "void" agreement is "an agreement not enforceable by law", e.g. an agreement with an alien enemy, an agreement by way of wager. Such an agreement creates no legal rights and obligations on either side. It is, in fact, a mere nullity. A voidable contract is "an agreement which is enforceable at law at the option of one or more parties thereto, but not at the option of the other or others", e.g. a contract induced by fraud or misrepresentation. The peculiarities of a voidable contract are these: (i) it is valid and binding on both the parties so long as it lasts; (ii) the law gives an option to one of the parties to avoid it, if he so chooses; (iii) the party entitled to avoid the contract is not bound to avoid it but may affirm it, in which case, (iv) the other party remains bound to carry it out as agreed. If the party chooses to affirm the contract or if he fails to use his right to avoid within a reasonable time so that the position of the parties is altered, or if third parties acquire rights in the goods before the contract is avoided, such party may lose his right to avoid the contract altogether. See Sale of Goods Act (seq.). A contract "becomes void" when it ceases to be enforceable at law. The reference here is to sec. 56, which deals with contracts which are valid and binding when made but subsequently "become void" because of a supervening illegality or impossibility.

Void and illegal contracts distinguished

A "void" contract must be distinguished from one which is "illegal" (in the sense that it is either prohibited by law or otherwise against the policy of law; sec. 23 seq.). Both contracts are unenforceable at law. The difference between the two, however, becomes clear when the legal effect of such contracts on collateral transactions is considered. The rule of law is that no contract which is designed to assist or promote an illegal transaction will be enforced at law. In other words, when a contract is illegal, collateral transactions depending thereon are also void (h). Thus in *Alexander v. Rayson* (i) two agreements of lease were effected of the same property but with different rentals, with a view to deceive the local authority as to the true rateable value of the premises. A dispute having arisen between the lessor and lessee, the Court held that, looking at the fraudulent object of the whole transaction, the Court will not assist the lessor in enforcing either the first or the second agreement against the lessee. As distinguished from this, is the case of a "wagering" agreement. Such an

(h) *Pearce v. Brooks*, L.R. 1 Ex. 213.

(i) (1936), 1 K.B. 169.

agreement is void (sec. 30 seq.) but not illegal. Collateral transactions arising from a wagering transaction, therefore, are not void. Thus there is nothing illegal in paying or receiving payment of a lost bet. Similarly, a broker can successfully maintain a suit against the principal for recovering his commission in respect of a wagering contract (j).

Communication of proposal, acceptance and revocation (secs. 3-4)

A proposal, an acceptance of a proposal and a revocation of proposal must be communicated by the party making them to the other, otherwise they are futile and do not give rise to legal rights or liabilities. Thus a reward being offered for finding out lost goods, a finder who finds them in ignorance of the advertisement is not entitled to the reward. In *Taylor v. Laird* (k) T being engaged to command a vessel belonging to L, threw up the job but worked on the ship and helped to bring it home. Held, he was not entitled to be paid for such services, as there was no proposal communicated by him to L, which L had the opportunity to reject. Sec. 3 lays down how communication is made. It is made (a) by some act or omission of the party concerned by which he intends to communicate such proposal, acceptance or revocation, or (b) which has the effect of communicating it. In the last cl. "or" is generally regarded as incorrect; the correct word being presumed to be "and" (l). However, there is English (m) as well as Indian authority (n) for holding that a revocation of a proposal before acceptance, is valid, though the knowledge of the revocation was obtained by the offeree from a stranger. Whether in a given case a proposal, etc. has been communicated is a question of fact. Difficulties arise in this connection where a proposal consists of a multiplicity of terms, e.g. a railway or ship ticket, an invoice, a railway receipt for goods. The rule laid down in such cases is that it is always a question of fact, whether a person accepting such document had notice of all the terms embodied therein. If (i) the terms relate more or less, to the subject-matter of the contract, and (ii) are of a usual kind, acceptance of the document would amount in law to the acceptance of terms, (iii) provided attention of the person has been duly drawn to the existence of the terms.

In *Henderson v. Stevenson* (o) a steamer ticket on the face of it only bore the words "Dublin to Whitehaven". The conditions at the back provided that the Company would not be liable for loss of or injury to luggage. Luggage was lost through the company's negligence. Held, the company was liable as the terms at the back were not communicated to the passenger. Similarly, in *Richardson v. Rowntree* (p) where the terms limiting the company's liability for injury to passenger, were printed on the face of the ticket, but in small type and were further obliterated by a stamp placed across them, it was held that there was no communication of the terms. It would be otherwise if pointed attention is drawn to the terms. Notice in this connection, that inability to read is no excuse (q).

Communication when complete (sec. 4)

The sec. considers when a communication can be said to have been completely made. Three rules are laid down: (i) a person making an offer is considered in law as continuously making it, till it reaches the offeree.

(j) *Daya Ram v. Murlidhar*, 49 All. 926.

(k) 25 L.J. Ex. 322.

(l) See *Pollock and Mulla, Indian Contract Act*, p. 31.

(m) *Dickinson v. Dodds*, 2 Ch. 463.

(n) *Papa Naidu v. Muniswami*, 46 Mad. 30.

(o) L.R. 2 H.L. 470.

(p) (1894). A.C. 217.

(q) *Mackillican v. Com. Messageris*, 6 Cal. 227.

Therefore, as the sec. lays down, the communication of a proposal is complete only when it comes to the knowledge of the person to whom it is made, i.e. when the letter containing the proposal reaches the offeree. (ii) The same is true of communication of acceptance. This however has two aspects, viz. as against the proposer and as against the acceptor. The sec. lays down that communication of acceptance is complete (a) as against the proposer, when it is put in course of transmission to him, so as to be out of the power of the acceptor, i.e. when the letter of acceptance is posted, and (b) as against the acceptor, when it comes to the knowledge of the proposer, i.e. when the letter of acceptance is received by the proposer. Notice that there is always an interval of time during which an acceptance made, though binding on the proposer, is still not binding on the acceptor. (iii) As regards revocation, the sec. lays down that it is complete (a) as against the person who makes it, when it is put in course of transmission to the other party, so as to be out of the power of the person revoking, i.e. when the letter of revocation is posted, (b) as against the person to whom it is made, when it comes to his knowledge, i.e. when the letter of revocation is received by the addressee. The importance of the sec. arises from the fact that a proposal or acceptance once made can be revoked only under certain conditions. Shortly speaking, a proposal cannot be revoked after it is accepted by the other side, because thereupon an agreement or a contract comes into being. Similarly, as regards an acceptance also. It is therefore necessary to know, when a proposal, acceptance or revocation is completely made. The sec. is designed to make this clear.

As regards (ii) above, notice that posting the letter of acceptance will bind the proposer, even if the letter is delayed in post or even if it miscarries. In *Household Fire Insurance Co. v. Grant* (r) the company had posted a letter of allotment to the defendant who had applied for shares. Through no fault of the company, however, the letter never reached the defendant. *Held*, he was liable as a shareholder of the company. If the letter of acceptance is misdirected through the fault of the acceptor, there would, in law, be no communication of the acceptance; but if the wrong address is furnished by the proposer himself, he will be bound. Similarly, if the method of acceptance is prescribed by the proposer, an acceptance, accordingly, will bind him, though the letter of acceptance never in fact reaches him (s). A good illustration of the importance of the provision is the case of *In re London and Northern Bank* (t) where A having applied for shares in a company, withdrew the offer by a letter of the 26th October which reached the company at 8-30 a.m. on the 27th October. At 7-30 a.m. on that day, the company had already resolved to allot the shares to A; but the letter of allotment was not posted till after 8-30 a.m. *Held*, the revocation was good. As regards (iii), notice that revocation is not complete till it is communicated to the other party. In *Byrne v. Von Tienhoven* (u) A from Cardiff on 1st October made an offer to B in New York asking for reply by cable. B received the offer on the 11th and at once cabled acceptance. In the meanwhile A, on the 8th October, had posted a letter revoking the offer. *Held*, the revocation was bad.

Where a contract is made by post, it is clearly the law that the acceptance is complete as soon as the letter of acceptance is put in the post box and that is the place where the contract is made. But there is no such clear rule where the contract is made by 'phone or by teleprinter. Communication in such a case is instantaneous and therefore if acceptance is not in fact communicated to the offeror, e.g. by the telephone suddenly going "dead", there will be no contract (u1).

(r) 4 Ex.D. 216.

(s) *Adams v. Lindsell*, 1 B. & Ald. 681.

(t) (1900), 1 Ch. 220.

(u) 5 C.P.D. 344.

(u1) *Entoris Ltd. v.*

(1955) 2 All E.R. 493.

Revocation, when can be made (sec. 5)

The importance of the above discussion arises from the question, when can a proposal, acceptance or revocation be revoked? This is answered by sec. 5, which lays down the following rules: (i) a proposal may be revoked at any time before communication of the acceptance is complete as against the proposer, i.e. (in terms of sec. 4), before the letter of acceptance is posted; (ii) an acceptance can be revoked at any time before the communication of the acceptance is complete as against the acceptor, i.e. before the letter of acceptance reaches the proposer. The reason for (i) is that whoever makes an offer, does not thereby agree to keep the offer open for any period. An offer therefore can always be revoked any time before the offeree has accepted it. *Re London and Northern Bank's case* (supra) is an illustration of the point.

In *Routledge v. Grant* (v), A offered to B to purchase his house giving him 6 weeks for answer. B accepted the offer but with material alterations. A thereupon withdrew the offer. B thereafter accepted A's offer as originally made, within the period of six weeks. *Held*, there was no contract. Similarly, at an auction sale, a bid can always be withdrawn, before the fall of the hammer. As regards (ii), an acceptance sent by post can be validly revoked by a telegram which reaches the proposer before the letter of acceptance.

Proposal, how revoked (sec. 6)

A proposal may be revoked in any one of four ways: (i) by notice of revocation, (ii) by lapse of time, (iii) by the failure of the offeree to fulfil a condition precedent to acceptance, and (iv) by the death or insanity of the proposer coming to the offeree's knowledge before acceptance. As to (ii) above, it has been held, where shares were applied for in June, and they were not allotted till November, that the offer had lapsed (w). Notice that an offer with a statement that it is open for acceptance till a certain date, does not bind the offeror to keep it open till that date, there being no consideration for such a promise (x). It only means that it will lapse after that date. An illustration of (iii) above, may be the following: A proposes to buy B's property if B will send the title deeds. If no title deeds are sent by B, A's offer will stand revoked. Similarly a conditional offer to pay a certain amount, made by the management of an industry to a Trade Union, has been held to lapse when the condition is not accepted (w1). As to (iv), notice that in English law, knowledge of death or insanity is not necessary before an offer is revoked in such cases.

Essentials of acceptance (sec. 7)

In order to amount to a valid acceptance, it must fulfil the following conditions: (i) it must be absolute and unqualified; (ii) it must be expressed in some usual and reasonable manner; (iii) if the offeror has prescribed a manner of acceptance, it must be made in such manner; (iv) if it is not made in such manner, the offeror has the right to reject the acceptance, but (v) if he does not notify to the acceptor his rejection of such irregular acceptance, the offeror is deemed in law to have accepted the imperfect acceptance. To this must be added a further condition, viz. (vi) that it should be duly communicated to the offeror. Whether an offer which has been made, has been accepted or not, is always a question of fact.

(v) (1828), 4 Bing. 653.

(w) *Ramsgate Hotel v. Montefiore* (1896),
L.R. 1 Ex. 109.

(w1) *Pepraich Sugar Mills v. Pepraich
Majdoor Union*, A.I.R. (1957) Cal. 95.

(x) *Dickinson v. Dodds*, 2 Ch.D. 463.

In *Harvey v. Facey* (*supra*), Facey's reply telegram quoting lowest price, was not an acceptance of the offer to buy and therefore it was held that there was no concluded contract. Whenever acceptance is alleged, however, it must fulfil all the conditions laid down by the sec. Thus as to (i), addition of further terms by way of acceptance is not acceptance. An offer to purchase goods to be ordered out from Europe, accepted with addition "free Bombay Harbour and interest", does not produce a concluded contract (y). Such an acceptance is, in effect, a "counter offer", which the offeror may or may not accept. Similarly, where a proposal to insure is accepted "subject to payment of premium", no insurance is effected nor does a contract to insure arise, till premium is paid and accepted (z). Note, however, that where the added terms are what the law itself implies in the proposal, the acceptance is in order. Thus where an offer to sell immoveable property was accepted, "subject to title being approved", it was held to be a good acceptance (a). A "provisional acceptance", subject to further confirmation is no acceptance (b).

As to (ii) above it has been held that a proposal conveyed by post is properly accepted by post. Notice that the sec. does not authorise a proposer to dictate the terms of rejection. A proposal with an intimation that the offeror will treat the same as accepted if no reply to the contrary is received within an intimated time, does not become a contract because no reply is received within the fixed time (d).

Articles of agreement sometimes provide for the "agreement" to be embodied in a formal document. The rule of law in such cases is that if the intention of the parties clearly appears to be that no concluded contract should be deemed to have been arrived at till the "agreement" is formally drawn up and, properly signed by the parties, the Court will not hold the parties bound by a contract, till such a document is formally executed by them. On the other hand, if it appears that the parties had already arrived at a concluded contract, but had desired that the terms should be reduced to writing and signed by themselves, in order to better preserve the evidence thereof, the fact that no such document was subsequently signed, will not prevent a contract from coming into existence (c).

Acceptance, how made (sec. 8)

An acceptance can be made (i) orally or (ii) by writing or (iii) by conduct. Thus taking a seat in a tram car is an acceptance of the company's proposal to carry passengers at the scheduled rates. Sec. 8 mentions two particular instances of acceptance by conduct. According to the sec., (i) the performance of the conditions of a proposal and (ii) the acceptance of the consideration for a reciprocal promise, offered with the proposal, amount to acceptance of a proposal. Cl. (i) above refers to such cases of *standing offers* as an advertisement for reward for finding a lost article. In such a case, the finding of the article in pursuance of the advertisement, operates as an acceptance of the offer.

In the *Carbolic Smoke Ball Co.'s case* (e) an old lady contracted influenza after using certain medical preparation (called "Carbolic Smoke Ball"), prepared by the defendants, who had publicly offered a reward (by way of puffing) for anyone contracting such disease after use of the said balls. Held, there was a good contract and the defendants were liable. Similarly, where a grand-aunt agreed to purchase immoveable property for her grand-niece, if she and her husband after marriage, resided with her and they accordingly did so, held, the condition being duly performed, a com-

(y) *Haji Mahomad v. Spinner*, 24 Bom. 510.
 (z) *Canning v. Farquahar*, 16 Q.B.D. 727.
 (a) *Hussey v. Horne Payne*, 4 A.C. 311.
 (b) *Somasundaram v. Prov. of Madras* (1947), 1 M.L.J. 123.

(c) *Ridgway v. Wharton*, 6 H.L.C. 238.
 (d) *Felthouse v. Bindley* (1862), 11 C.B. N.S. 869.
 (e) *Carlill v. Carbolic Smoke Ball Co.* (1893), 1 Q.B. 256.

plete contract had come into existence and the niece was therefore entitled to the possession of the house which the grand-aunt had purchased (f). Similarly, an acceptance by an insurance company of a cheque from the assured as payment of first premium, creates a completed contract of insurance though there has been no communication by the company to the assured of the acceptance by the company of the assured's proposals (g). In a Madras case an insurance company wrote to the assured whose policy had lapsed to remit the premium amount before a certain date so that the insurance protection may continue to be bestowed on the policy. The assured remitted the moneys by money order before the date mentioned by the company but died the day after and before the moneys reached the company's hands. On a claim for policy moneys, *held* that sending of money by money order must be taken to be the probable mode of payment intended under the circumstances and that therefore as soon as the moneys were paid in the Post Office, following the demand, the policy must be deemed to have been revived (h).

The meaning of cl. (ii) is a little obscure. It is intended to cover cases, e.g. where a person having an overdraft account with a bank, operates on the account, after notice that the rate of interest with regard to such account has been enhanced. Goods sent on approval, which are kept by the offeree, implies a promise to pay the price thereof.

Promise : express or implied (sec. 9)

A promise may either be (i) express or (ii) implied. The sec. provides that in so far as a proposal or acceptance is made in words (spoken or written) the promise is said to be express; (ii) in so far as these or any one of them is made otherwise, e.g. by conduct, the promise is said to be implied. Cases of such implied promises are the implied promise to pay interest at a certain rate on amount due at the foot of the account, by acceptance of "ankadas" charging such interest for a number of years, without any objection (i). The "implied promise" here considered differs from "a promise implied by law" which is considered by secs. 68-72. In the latter class of case there is no promise in fact but the law implies one (see seq.).

Foreign Contracts

The nature and extent of the obligation under a foreign contract has to be determined by the foreign law where the contract took place and was to be executed (j). The law for assessment of damages in case of a breach of a foreign contract has also been recently held to be the appropriate foreign law (k). Procedural rules to be followed are of the "lex forie", i.e. of the place where the contract or its breach is sued upon.

It has been held in Bombay that where a question arises as to whether the incidents of a contract should be governed by the law of one country or another, the general rule is that the rights and incidents are governed by the laws of the country where the contract is made. Where therefore the law of one province of British India was distinct from the law of another province, *held*, the two provinces must be regarded for the purpose of this rule as foreign countries (l).

(f) *Malraju v. Venkatanarasinha*, 18 Bom. L.R. 651.

(g) *Hindustan Co-operative Insurance Co. Ltd. v. Syam Sunder*, 56 C.W.N. 418.

(h) *Haroon Bibi v. United India Life Insurance Co. Ltd.* (1946) 2 Mad. L.J. 233.

(i) *Jagmohan v. Manikchand*, 7 M.I.A. 263.

(j) *Fergusson v. Fiffi*, 8 E.R. 49.

(k) *J. D'almaida v. Sir F. Backer & Co.* (1953), 2 All E.R. 288.

(l) *Shanker v. Maneklal*, 42 Bom. L.R. 873.

Construction of contract: A contract in writing must be generally construed according to the actual tenor of the words, and no supposed intention of parties can afford a safe construction. Further, no unexpressed condition can be implied in a contract in writing, unless such term is necessary in order to give the contract, such efficacy as both the parties must in all reason intended it to have (11).

CHAPTER III

ESSENTIALS OF A VALID CONTRACT

Essentials of a valid contract (sec. 10): This sec., in many respects, is one of the most important in the Contract Act, as it defines what are the fundamentals of every contract. According to the sec. "all agreements are contracts, if they are made (i) by the free consent of parties, (ii) competent to contract, (iii) for a lawful consideration and (iv) with a lawful object and (v) are not declared (by the Contract Act) to be void". These five basic requirements of every contract are considered in detail by the succeeding secs., e.g. (i) by secs. 13-22, (ii) by secs. 11-12, (iii) and (iv) by sec. 24, and (v) by secs. 25-30. It should be noticed that these five are not the only requirements of a valid contract. As the second cl. to sec. 10 points out, the sec. is not intended to abrogate special rules of law, which other Acts have prescribed for particular contracts. Thus under the "Transfer of Property Act", sales, mortgages, leases, gifts, etc. of immoveable property above a certain value, are required to be in writing signed by the parties concerned and registered and in certain cases attested by witnesses. Similarly, under the "Registration Act", certain transactions relating to immoveable property are required to be registered in order to be valid. These provisions remain operative wherever they are properly applicable.

Competency to contract (secs. 11-12)

According to sec. 11, every person is competent to contract (i) who is of the age of majority, according to the law to which he is subject, (ii) who is of a sound mind, and (iii) who is not disqualified from contracting by any law to which he is subject. The above three essentials of "competency" may be considered separately.

Majority

According to the Indian Majority Act (IX of 1875), a person is deemed to have attained majority (i) when he completes 18 years. (ii) Where, however, a guardian of his person or property or both has been appointed by a Court of Law (or where, his property has passed under the superintendence of the Court of Wards), such a person attains majority on completion of 21 years. (iii) The Act lays down, however, that the above limits are not to affect the question of capacity with regard to marriage, dower, divorce and adoption. The capacity in these cases is to be determined by the special rules of law applicable to parties, according to the respective community to which they belong. Notice that the sec. requires majority to be determined by the law to which the person is subject. The Indian Major-

(11) *Navnitlal & Co. v. Keshavchand & Co.*, A.I.R. (1956) Bom. 157.

rity Act applies only to persons domiciled in India. A person with a foreign domicile, therefore, will be governed by that foreign law with regard to majority.

Thus where a Hindu widow whose domicile of origin was Kolhapur and who was above 16 but below 18 years, passed a bond in favour of a creditor at Kolhapur, it was held that, if the widow's domicile was Kolhapur, she would be bound by the contract, because according to Kolhapur law, the age of majority was 16 years. As, however, a woman on marriage acquires the domicile of her husband (who was, in this case, a British Indian subject), it was further held that she was not liable on the bond, as she was a minor according to British Indian law and therefore incapable of contracting (m).

Minor's contract void

The importance of the question of majority arises from the fact that according to Indian Law as it now stands, it is settled that a minor's contract is absolutely void and not merely voidable. This was decided by the Privy Council in the leading case of *Mohori Bibee v. Dharmo das Ghose* (n) where a mortgagee of property belonging to a minor had filed a suit to recover his mortgage amount and for sale of the property in case of default. The Privy Council held that whatever may be the English Law on the subject (and at that time, a minor's contract according to English Law, was voidable only and not void), according to sec. 11 of the Contract Act, by which the parties were governed, a minor was "incompetent to contract". They held therefore that the minor's contract was void altogether and not merely voidable and that the mortgagee could not recover the moneys advanced by him to the minor nor could he have his property sold under his mortgage. Under English Law also, as it stands at present, a minor's contract is now void.

Consequences of the above

A minor's contract being void, the following consequences result: (i) Moneys advanced to a minor on a promissory note or otherwise, cannot be recovered back (supra). Similarly, a guarantee for an overdraft account in favour of a minor cannot be enforced against the guarantor (o). (ii) A minor's contract being void, it cannot also be specifically enforced against the minor, under the Specific Relief Act. (iii) The fact that the minor misrepresented his age and thus, by means of fraud and misrepresentation, induced the other party to enter into a contract with him, cannot be availed of, to make the minor liable on his contract (p). (iv) Estoppel, under sec. 115 of the Evidence Act, cannot be pleaded against a minor, in order to enforce a contract against him (q). Estoppel is a rule of evidence, which prevents a person from disputing the truth of what he has represented, when another person has acted on the faith of such representation to his disadvantage. This rule cannot be invoked against a minor (r). (v) A minor's contract being void, it cannot be ratified by the minor on attaining majority. Thus a promissory note passed by a minor after attaining majority, in settlement or renewal of another promissory note passed by him during his minority, cannot be enforced, because there is no consideration for the second note (s). It would be otherwise if fresh consideration is passed at the time of the

(m) *Kashiba v. Shripat*, 19 Bom. 697.

(n) (1903). 30 I.A. 114.

(o) *Coutts & Co. v. Browne Lecky* (1947), K.B. 104.

(p) *Gadigeppa v. Balangauda*, 33 Bom. L.R. 1313.

(q) *Balangauda v. Gadigappa*, 31 Bom. L.R. 340.

(r) *Sadik Ali v. Jai Kishore*, 30 Bom. L.R. 1346.

(s) *Indru v. Anthappa*, 16 Mad. L.J. 224.

second note. (vi) A contract cannot also be turned into a tort (i.e. a civil wrong, independent of contract), in order to make a minor liable. Thus fraud or deceit is a civil wrong for which damages are recoverable. On a contract induced by fraud being unenforceable against a minor, the plaintiff cannot turn round and file a suit against him for damages for deceit, for having induced the plaintiff to enter into the contract by such means (t).

Exceptions

A rule so strict, naturally has certain exceptions to it. Thus (i) though a contract cannot be enforced against a minor, a minor can take a benefit under a contract and can enforce such contract for his benefit. Thus moneys advanced by a minor can be recovered by him by suit. Similarly, a minor purchaser or mortgagee can enforce the sale or mortgage (u). Can a minor take a lease? The Patna High Court has answered the question in the negative (v). The point however is doubtful. (ii) Contracts entered into by a guardian of a minor, provided they are within his powers as such guardian, and further, are for the benefit of the minor, are binding on the minor and can be enforced against him. Thus a contract for sale of immoveable property entered into by the guardian of a minor with the sanction of the court can be enforced by and against the minor (w). Note however that a guardian has no power to purchase property for and on behalf of a minor (x). Similarly, a contract of service entered into by a guardian on behalf of a minor is void and not enforceable at law (y). (iii) A contract for supply of "necessaries" to a minor or to those who are dependent on him can be enforced against him, not personally, but so far as his property may extend (sec. 68 seq.). (iv) An agreement for marriage of a minor daughter made by a guardian, if broken, has been held to furnish a ground to the daughter to claim damages against the defaulting person as on a breach of contract (see *Rose v. Joseph Gonsalves* (z) where the decision is placed on the ground of special custom). The rule has been extended to the case of Hindus also (a). (v) Where under sec. 41 of the Specific Relief Act, a minor sues to have a document, e.g. a sale deed or a mortgage deed, etc. made by him, declared void and for cancellation of the same, the Court can, before granting such equitable relief to the minor, require him, as a condition precedent, to do equity himself, i.e. to pay back to the other party, as and by way of compensation, all benefit he has obtained under the transaction sought to be set aside (b). (vi) A minor, under sec. 184 of the Act, can be appointed an agent. (vii) A minor can, under sec. 30 of the Partnership Act, be admitted to the benefits of a partnership.

Soundness of mind (sec. 12)

According to the sec., a person is said to be of a sound mind, for the purpose of entering into a contract when (i) at the time when he entered into it, (ii) he is capable of understanding it, and (iii) of forming a rational judgment as to its effect upon his own interests. It follows from the above that a lunatic can enter into a valid contract during a lucid interval. Con-

(t) *R. Leslie v. Sheill* (1914), 3 K.B. 607.
 (u) *Ulfat Raj v. Gouri Shankar*, 33 All.
 657.
 (v) *Pramala v. Jogeshwar*, 3 Pat. L.J. 518.
 (w) *Etwarie v. Chandra Nath*, 10 Cal.
 W.N. 763.
 (x) *Mir Sarwarjan v. Fakruddin*, 39 I.A.

(y) *Raj Rani v. Prem Adib*, 51 Bom. L.R.
 256.
 (z) 48 Bom. 673.
 (a) *Khimji v. Lalji*, 43 Bom. L.R. 35.
 (b) *Kamta Prasad v. Shco Gopal*, 26 All.
 342.

versely, a contract entered into by a sane person, while under the influence of drink is unenforceable against him. As in case of a minor, a contract by an insane person is void and cannot be enforced against him, though he can enforce and take a benefit under a contract. A lunatic of whose estate a committee or manager has been appointed, is incapable of contracting even during lucid intervals, by reason of the special provisions of the Lunacy Act.

Disqualified persons

The third requirement of "competency to contract" is that the person should not be "disqualified" from entering into a contract by any law which is properly applicable to him. Thus alien enemies during war are disqualified from entering into contracts with the Crown's subjects. Similarly, statutory bodies like Municipalities cannot enter into contracts which are beyond their statutory powers. An incorporated company also cannot enter into a contract which is *ultra vires* the memorandum. Notice that a woman in Indian Law is under no disqualification by reason of her sex as regards entering into a contract. It was otherwise under English Law till recent times.

Consent (sec. 13)

The second requirement of a valid contract is "free consent". Before "consent" can be "free", however, one has to make sure whether there has been any "consent" at all. What is "consent" is defined by sec. 13. According to the sec., two persons are said to "consent" when they "agree upon the same thing in the same sense". This is called in English Law "*assensus ad idem*". Whether there is such a "consent" in a given case, is a question of fact.

Absence of "consent" may arise from a variety of causes: (i) by reason of an error as to the nature of the "contract" itself; (ii) by reason of an error as to the person with whom the "contract" is entered into; (iii) by reason of an error as to the subject-matter of the "contract". In all these cases, there is not merely a void contract, but no contract at all, because in the law of contract "*assensus ad idem*" is a condition precedent to any contract coming into existence at all.

Thus where an aged person signed a bill of exchange as drawn, under the wrong impression that it was only a letter of guarantee which he was signing, it was held that a holder in due course of such a bill, had no rights as such, "as the writer's mind did not go with his pen" (c). Similarly, in an Indian case, where a release of debt was signed by a person under the erroneous belief that it was merely an assignment of the property of the debtor to trustees, for the benefit of creditors, it was held that there was no contract, as there was an error as regards the nature of the transaction (d).

Error as regards the identity of the other party to the contract is well illustrated by the case of *Cundy v. Lindsay* (e), where one Blankarn, by closely imitating the signature of the well-known firm of Blankiron and Co., ordered out goods from a firm, which, on being thus supplied by the latter, were promptly sold by Blankarn to the defendants, who paid value therefor, without notice of the fraud. Blankarn having disappeared with the money, it was held, in a suit brought by the suppliers against the defendants, that the goods still remained the property of the plaintiffs, there being no "contract" between them and Blankarn for the sale of the goods in question.

Error may also arise as regards the subject-matter of the contract. Thus where there was a "contract" for the sale of goods arriving per "ex good ship Peerless", and there were two ships of that name and the parties had in mind, different ships at the

(c) *Foster v. Mackinnon*, I.R. 4 C.P. 704.

(d) *Oriental Banking Corporation v. Fleming*, 3 Bom. 242.

(e) (1878), 3 App. 451.

time of entering into the "contract", held, there was no "contract" as there was no "consent" between the parties (f). Notice that cases falling within the principle of the sec. have nothing to do with either fraud or misrepresentation, which are considered later.

Free consent (sec. 14)

According to the sec., consent is said to be free when it is not caused by (1) coercion, (2) undue influence, (3) fraud, (4) misrepresentation or (5) mistake as defined in subsequent secs. Consent is said to have been caused by any of the above means, if it would not have been caused but for their existence. Whether consent in a given case is caused by any of the above means is a question of fact. The test in all the above cases is, whether consent was free and voluntary; in other words, was the person consenting a free agent? If he was not, the contract cannot be made binding on him. The above causes are next considered in detail.

Coercion (sec. 15)

The sec. defines "coercion" as (i) "committing or threatening to commit any act forbidden by the Indian Penal Code or (ii) the unlawful detaining or threatening to detain any property to the prejudice of any person whatever (iii) with the intention of causing any person to enter into an agreement". (iv) It is immaterial whether the Indian Penal Code is or is not in force at the place where coercion is employed. This is called "duress" in English Law which, however, does not include illegal detention of property.

Thus executing a bond under fear of assault, would be under the sec. Where a widow agreed to adopt a boy, under the threats of her castemen who refused to carry the dead body of her husband, if she did not sign the document of adoption, it was held that coercion was employed (g). A release signed by a wife, under her husband's threats to commit suicide, is also within the sec. (h).

As regards the second clause, notice that the property detained may belong to any person, the unlawful detention may also cause damage to any person,—not necessarily to the person "agreeing".

Where an agent refused to hand over the books of account to the principal, unless the latter agreed to a settlement of accounts, which he eventually did, it was held that the settlement was bad as "coercion" had been employed by the agent (i). In this connection notice that a mere threat of criminal prosecution is not enough, but where the circumstances are such that the threat deprives the person of his free will altogether, coercion will be held proved. Thus where a son fabricated his father's signature on promissory notes and thus defrauded bankers, a settlement by the father with the bankers, who otherwise threatened to prosecute the son, was relieved against, the father, under the circumstances, not being regarded as a free agent. As the sec. says, it is not necessary that the Indian Penal Code should be applicable at the place where coercion is employed. If the act would be an offence under the Indian Penal Code, it would amount to coercion, e.g. a contract entered into on the high seas through criminal intimidation which according to English Law is not an offence but is one according to the Indian Penal Code (see illustration to sec.).

Undue influence (sec. 16)

Cl. (1) of sec. 16 defines "undue influence" as follows: "a contract is said to have been caused by undue influence (i) when the relations

(f) *Raffles v. Wichelous* (1862), 2 H. & C. 906.

(g) *Ranganayakam v. Alwar Setti*, 13 Mad. 214.

(h) *Amecrajie v. Sheshamma*, 41 Mad. 33.

between the parties are such that one is in a position to dominate the will of the other and (ii) uses that position (iii) to obtain an unfair advantage over the other". The second cl. defines when a person is deemed to be "in a position to dominate". It is so "(i) where he holds a real or apparent authority over the other or (ii) where he stands in a fiduciary relation to the other or (iii) where he makes a contract with a person whose mental capacity is temporarily or permanently affected by age, illness or mental or bodily distress". The third cl. lays down a rule of evidence. It says: "(i) where a person in a position to dominate the will of another enters into a contract with the other and, (ii) the transaction appears on its face or on evidence led, to be unconscionable, the burden of proving that the contract was not caused by undue influence shall be on the person in the dominant position". The above three cls. must be clearly distinguished. The first defines undue influence, the second lays down a rule of presumption, while the third lays down a rule as regards burden of proof, when the transaction is impugned in a Court of Law.

As regards cl. (i), observe that all the three conditions laid down by the cl. must be fulfilled before a contract can be set aside on the ground of undue influence. Firstly, the relationship must be such that one party is in a position to dominate the will of the other. Secondly, such party must have used that dominant position, and thirdly, he must have, by such use, obtained an unfair advantage over the other. If any one of the three elements is absent, the transaction cannot be set aside on the ground of undue influence. Thus, a bargain between an ordinary creditor and debtor cannot be challenged on the ground of its hardness, the position of the parties being equal. Similarly, an advantage obtained by a person standing in a fiduciary position to another, from such other, cannot be attacked, when such latter person has acted in the matter under independent advice. Lastly, a transaction which is absolutely fair and honest will not, except in some cases, be set aside, because one of the parties was in a dominant position quâ the other. In short, unconscientious use of superior power, and not fraud, is the principle underlying the sec. The principle is not confined only to the class of persons mentioned in the sec. As Lord Kingsdown pointed out in *Smith v. Kay* (j) "it extends to all cases where influence is acquired and abused, where confidence is reposed and betrayed". The principle is one of equity and has been made applicable, both in England and India, not only to cases of contracts but also to the case of gifts (k).

Thus in *Alkard v. Skinner* (l) a gift by a nun to the mother-superior of an Anglican convent was set aside, it having been found that the gift was made by the donor solely as the result of the spiritual influence which the other exercised over her. Similarly, in *Huguein v. Beasley* (m) a voluntary settlement made by a widow to a clergyman who was managing her affairs was set aside for a similar reason. In *Channel v. Bruce* (n) two sisters with leanings towards spiritualism, under the influence of a "medium", who claimed to be inspired by a "Grey Father", fought an accident claim and obtained a decree for £1,500. Under the "advice" of the "Grey Father", as conveyed by the "medium", and under the threat of the spirit world becoming angry, they ultimately parted with £400 by way of gift to the "medium". He, however, was not allowed by the Court to keep the money but was ordered to pay it back to his donors.

(i) *Muthiar v. Karrupan*, 50 Mad. 786.

(j) (1859), 7 H.L.C. 750.

(k) *Lingo v. Dattatraya*, 39 Bom. L.R.

(l) 36 Ch.D. 145.

(m) 14 Vcs. 273.

(n) 83 Sol. J. 136.

Following the above rulings, the Bombay High Court in *Raghunath v. Varjivandas* (o) set aside a gift made by a beneficiary under a trust to his trustee of a part of the trust funds, it being proved that the former had no independent advice in the matter. Similarly, where a gift of practically the whole of his property was made by an old man in favour of his guru, in order to obtain spiritual happiness in the next world, the Allahabad High Court set aside the gift (p). Notice in this connection that parents and spiritual and legal advisers (e.g. solicitors, managing clerks, etc.) have been held to be persons holding "real or apparent" authority, under cl. 2 of the sec. In these cases, therefore, independent advice is the *sine qua non* of the validity of both a contract as well as a gift. The relation of a guardian and a ward, of a *cestui que trust* and a trustee has been held to be of a fiduciary nature, i.e. of active trust. In these cases, therefore, not only *bona fides* but absolute removal from all undue influence must be shown. The relation of husband and wife (q), of master and servant and of creditor and debtor, however, has been held not to be such as necessarily to give rise to a presumption of domination under cl. (2) (a).

Mental or bodily distress under cl. (2) (b), is the common general head under which the majority of cases of undue influence are sought to be brought. Thus the case of *Ranganayakam v. Alwar Setti* (supra) (r) can fall under this also. Similarly, where an aged Brahmin made a gift of all his properties to a temple, which was in charge of the defendant and it was found that the donor was living in the defendant's house, was being fed and maintained by him and further that the defendant was also conducting with his own moneys a litigation of the donor, the Court set aside the transaction, as it was obvious that the defendant had the donor completely at his mercy (s). Notice in this connection, however, that a mere threat to prosecute is not enough to establish domination. It may, however, create a "well-founded terror" in the other person's mind, and if under such influence, a contract or gift is extracted, it will be liable to be set aside (t).

"Pardanashin"

"Pardanashin" ladies are a special class of persons who, by Indian Law, have been presumed to be ordinarily incapable of managing their own affairs, by reason of their special mode of life. "Pardanashin" here does not mean anyone who observes "Parda", but only those women who live in complete seclusion by reason of the custom of the community to which they belong. Thus a woman who goes to court to give evidence, who leases out her property and collects rents, takes advice of others outside her family, is not a "pardanashin" (u). Where a transaction is entered into with a "pardanashin" woman, e.g. a sale, mortgage, gift, release or a document is signed by her, the Privy Council has laid down in a number of cases that it is not enough to show that the transaction or deed was explained to her but it must be further shown affirmatively, that the same was fully understood by her, the burden of proving which, again, is on those who support the transaction or deed. Of course, it must also be clearly established that no undue influence was used and that she deliberately and of her own free will, entered into the same (v). The explanation must include all material points as well as the general nature of the transaction (w). It has been held by the Privy Council, however, that if the other conditions are satisfied, it is not absolutely necessary to prove in each case that the lady had independent advice (x). Notice that undue influence, in case of a "pardanashin" woman, may proceed from a person not a party to the transaction (y).

(o) 30 Bom. 578.

(p) *Mannu Sing v. Umadat*, 12 All. 523.

(q) *Howatson v. Webb* (1907), 1 Ch. 537.

(r) See p. 21 ante.

(s) *Sitalprasad v. Prabhulal*, 10 All. 535.

(t) *Mahomad Baksh v. Hussaini Begum*,
15 I.A. 81.

(u) *Ishmail v. Hafiz Boo*, 33 I.A. 86.

(v) *Kali Baksh v. Ram Gopal*, 41 I.A. 23.

(w) *Asgar Ali v. Dilroos Banu*, 3 Cal. 324.

(x) *Sunita Bala v. Dhara Sundari*, 46
I.A. 272.

(y) *Badiaatannissa v. Ambika Charan*, 18
C.W.N. 1133.

In *Bulzoor Rahim v. Shamsoonissa* (z), a suit was brought by a Mahomedan "pardanashin" lady against her husband, to recover government paper handed over by her to her husband to collect interest. The husband, however, claimed the same as under a sale for value. The plaintiff failed to prove her case. It was held, however, that the burden of proof was on the husband, and as he had failed to show affirmatively that the transaction was explained to and understood by the lady and that she was a free and voluntary agent, he was bound to return the paper to the plaintiff. In another case a "pardanashin" woman had made a gift of half her estate to the son of her lover. No undue influence was proved, but the lady had no independent advice. It was held however that such advice was not absolutely necessary and as all the other conditions were satisfied, the transaction was binding upon her (a). The Privy Council in a recent case *Inche Noriah v. Shukh Illie* (b) stated the rule as follows: Where the relations between the donor and the donee were, at or shortly before the execution of the gift, such as to raise a presumption that the donee had influence over the donor, the Court would set aside the voluntary gift, unless it was proved in fact that the gift was the spontaneous act of the donor, under circumstances which enabled the donor to exercise his independent will. They pointed out, however, that taking of independent legal advice was not the only way to rebut the presumption. In the above case, a Malayan woman of great age and wholly illiterate executed a deed of gift of landed property at Singapore in favour of her nephew, who had the management of all her affairs. Before executing the gift, the donor had independent advice from a lawyer who acted in good faith. He was not aware, however, that the gift constituted practically the whole of the donor's property and he did not bring home to her mind that she could more prudently and equally effectively, benefit the donor by bestowing the property upon him by will. Held, the gift should be set aside, as the presumption which arose was not rebutted. It is not necessary that the lady should understand every technical detail of the transaction, if she comprehends the substance of the bargain. If an important part of it, however, is not understood by her (e.g. a mortgage with a personal covenant of repayment, which latter is not understood by her), the transaction cannot be split into parts but the whole will fail (c).

The protection given by law to a pardanashin lady extends also to cases where ignorance and illiteracy is proved, exposing the woman concerned to the danger and risk of an unfair deal. The protection of law cannot be denied to such a woman, simply on the ground that she is not strictly pardanashin. Factual understanding of the document will be required to be proved in such cases also (c1).

"Expectant heirs"

These are persons who, expecting a large reversion to fall in for their benefit at any time, run into improvident bargains with regard to them with unscrupulous money-lenders. "Expectant heirs" was an old head of English Equity, in which relief was granted as a matter of course. This, however, would not necessarily be so in India, where we are strictly governed by sec. 16 of the Act.

Burden of Proof

Cl. (3) of sec. 16 lays down a rule of evidence and throws the burden of proving absence of undue influence on the party affirming the transaction (and not on the party alleging undue influence), where (i) the party is in a position to dominate the will of the other as laid down in cl. (2) or other-

(z) 11 M.I.A. 551.

(a) *Kali Baksh v. Ram Gopal* (Supra).

(b) (1929), A.C. 127.

(c) *Hemchandra v. Suradhani*, 42 Bom. L.R. 993 (P.C.).

(c1) *Sonia v. Shaikh Moula Baksh*, A.I.R. (1955) Cal. 17.

wise and (ii) the transaction appears (on its face or on evidence led) to be unconscionable, i.e. inequitable.

Thus, where a Hindu heir, 16 years old, who had no means of existence, borrowed Rs. 3,700 to prosecute a claim and passed a bond for Rs. 25,000 to be paid on the receipt of the property, it was held that the transaction was unconscionable and could not be regarded as binding on the borrower (d). Similarly, where a profligate son of a wealthy father, aged 28, borrowed Rs. 500 on the terms that interest was to be paid at 37½ per cent, with six monthly rests, and further, that the moneys were not to be repaid for 3 years and even if repaid, interest at the above rate was to run for the agreed period, the transaction was set aside (e). Of course, in such cases the moneys actually advanced will have to be repaid but on reasonable terms as regards interest and other things.

Notice, however, that the mere fact that the bargain is evidently harsh will not necessarily invalidate it. Both the above conditions must be satisfied before the presumption raised by the cl. will apply.

Thus where a property was mortgaged for Rs. 5,000 and Rs. 1,250 in lieu of interest and it was further agreed that the whole amount was to be repaid in 75 instalments, each instalment in arrear to carry interest at 24 per cent and Rs. 100 were further retained by the lender as "Khichadi", i.e. bonus, it was held that the transaction could not be set aside, as both parties were money-lenders and as such, used to hard bargains (f). Similarly, an exorbitant rate of interest or compound interest is, by itself, not sufficient to invalidate a transaction under the sec. (g) [see also ill. (d)]. Where, however, the transaction falls under the Usurious Loans Act, relief against excessive interest can be granted under that Act.

Undue influence can be pleaded by way of defence, though the right to have the document declared void as plaintiff, on the ground of undue influence, may have become barred by Limitation (h).

Fraud (sec. 17)

The sec. defines fraud as consisting of certain kinds of acts mentioned therein, committed by a party to a contract, or his agent or by his connivance with a view to deceive another party to the contract or to induce him to enter into the contract. The acts are (i) suggestion of a fact of that which is not true, by one who does not believe it to be true; (ii) active concealment of a fact, by one having knowledge or belief of the fact; (iii) a promise made without any intention of performing it; (iv) any other act fitted to deceive; (v) any act or omission, which law specially declares to be fraudulent. The Explanation adds a rider to the above, viz. (vi) Mere silence as regards matters which may affect a party's willingness to enter into a contract is not fraud unless, (a) there is a duty to speak, under the circumstances, or (b) unless the silence is equivalent to speech.

Representations

A representation is a statement or assertion, made by one party to another, before or at the time of the contract, of some matter or circumstance relating to it (i). Such a representation may either (i) form a term of the contract or (ii) may, without actually forming a term of the contract, be the inducing cause of the contract. The point to notice here is that it is the latter case alone which is considered by secs. 16 and 17. The first case

(d) Chunni Kuar v. Rup Sing, 11 All. 57.

(e) Balkison v. Madanlal, 29 All. 303.

(f) Hari v. Rawji, 28 Bom. 371.

(g) Lala Bala Mal v. Ahmad Shah, 21 Bom. L.R. 558.

(h) Ranganath v. Govind, 28 Bom. 639.

(i) Benn v. Burness, 3 B. & S. 575.

is considered by secs. 11-17 of the Sale of Goods Act, where the distinction between terms which amount to warranties and conditions respectively is explained. Representations which do not fall under any of the above categories are of no legal consequence. Notice that the secs. deal with the question of fraud and misrepresentation in the making of a contract, and not in the carrying out of it. Fraud in carrying out a contract may lead to a claim for damages or to a criminal liability but it cannot make a contract voidable which is not voidable otherwise.

"Suggestio falsi"

Cl. (1) of sec. 17 refers to what is known in English Law as "*suggestio falsi*". Thus were the director of a company issued a prospectus which contained statements of fact which were false to his knowledge, it was held that a person who had taken shares on the faith of such prospectus was entitled to avoid the contract on the ground of fraud (j). Notice that a reckless mis-statement without caring to inquire whether it is true or false, is also fraud. Thus in *Rees Silver Mining Co. v. Smith* (k), the directors of a company issued a prospectus setting forth advantages which the proposed company would enjoy, without verifying the truth or falsity of these statements. Held, this amounted to fraud. Notice however that a statement of opinion, e.g. that the property is worth so much or a statement of intention is not a statement of fact. Similarly, if the statement, though false, is believed to be true, no case of fraud arises. A false statement deliberately made with the knowledge that it is false or without belief in its truth, is the basis of fraud. In *Derry v. Peek* (l), a tram company issued a prospectus stating that the company had the right to use steam power. The right could be exercised only with the consent of the Board of Trade. The latter refused their sanction and the company was wound up. Held, as the directors believed the statement to be true, they were not guilty of fraud.

"Suppressio veri"

Cl. (2) of sec. 17 refers to cases which are covered by what is called "*suppressio veri*". The emphasis is on the words "active concealment" as contrasted with "mere silence" of the Explanation. If a horse with a cracked hoof is offered for sale and the hoof is stuffed up to defy detection, a purchaser who is deceived thereby is entitled to avoid the contract on the ground of fraud. Here an active or positive step is taken to deceive the prospective purchaser. As to cl. (3) it has been held that purchasing goods without any intention of paying for them entitles the seller to avoid the contract (m). Cl. (4) is intended to cover all possible forms of deceit, which are countless. Cl. (5) refers to certain statutory obligations as regards disclosure. Thus under sec. 55 of the Transfer of Property Act, the seller of immoveable property is bound to disclose to the buyer all material defects in the property sold, of which the seller is aware and the buyer is not. Similarly, under the same sec., the buyer is bound to disclose to the seller all material facts as to the extent or nature of the seller's interest in the property, of which the buyer is aware but the seller is not. Omission to make such disclosure is made fraudulent. An innocent omission in such cases, therefore, will also amount to fraud.

(j) *Edington v. Fitzmaurice* (1885), 29 Ch. D. 459.

(k) 4 H.L. 64.

(l) (1889), A.C. 337.

(m) *Clough v. L.N.W. Rly.*, L.R. 7 Ex. 21.

Fraudulent silence

The Explanation to sec. 17 deals with cases of what is called "fraudulent silence" or what is sometimes called "*constructive fraud*". Generally there is no duty cast by law on a party to a contract to make a disclosure to the other party, of facts within his knowledge, which may affect the other party's willingness to contract. Thus in an American case (n), a failure to disclose by a party to a contract for sale of tobacco, of the cessation of the American Civil War of 1812, was held not to be sufficient to entitle the other to avoid the contract. Two exceptions to this rule, however, are recognised: (i) where circumstances create a duty to speak and (ii) where silence is equal to speech. The first refers to contracts which are called contracts "*Uberrimae fidei*". These are contracts in which the law casts a duty of abundant disclosure on one of the parties thereto, the reason being that owing to peculiar circumstances, that party has means of knowledge which are not accessible to the other. They are called contracts of abundant confidence. No element of fraud or misrepresentation is necessary to give rise to a right of a rescission; mere absence of sufficient disclosure is enough to entitle a party to avoid such contracts. They include contracts between parent and child (see illustration), a guardian and ward, contracts of fire, marine and life insurance, and in fact all contracts of insurance, contracts of family settlement, for sale of land, and to some extent, contracts for allotment of shares in a company. Contracts of suretyship and of partnership are also sometimes included but they depend on a different principle. Insurance contracts require the utmost good faith and the most complete disclosure of all material facts by the assured to the insurers. If such disclosure is not made, the insurers are entitled to avoid the contract, though the omission may have been unintentional or accidental.

Thus in *Ionides v. Pander* (o) a marine insurance policy on goods was set aside as the fact of over-valuation of the goods was not disclosed to the underwriters. Similarly, in a life policy, an answer to a question which is true, so far as it goes, but is not the whole truth, may vitiate a policy. Thus in *London Assurance Co. v. Mansel* (p) to the query, whether a proposal has been made to other offices, and declined, the assured answered that he was insured at two offices, but failed to disclose that at one of them he had attempted to raise the insurance, but it was declined, held, the company was not bound by the policy. As regards sales of land, it has been held that the failure on the part of the vendor to disclose onerous and unusual covenants in a lease, is sufficient to avoid the contract of sale of such a lease (q). As regards allotment of shares, law requires that those who issue prospectuses should state everything therein with strict and scrupulous accuracy. They must not only abstain from stating as a fact, that which is not so, but must not omit to mention any fact, which is within their knowledge and which might reasonably affect the mind of persons wishing to take up shares in the company (r). Notice that a statement true when made, but which subsequently becomes untrue, by change of circumstances, will entitle a party to rescind the contract (s).

The second class is exemplified by the illustration. If A buying a horse from B tells B that he will assume that the horse is alright, unless B denies it and B remains silent, his silence is equal to a positive statement that the horse is sound, which, if false to his knowledge, is fraud. Of course, fraud must have induced the contract. In *Peek v. Gurney* (t) a person who had bought shares from an original shareholder, was held not entitled to avoid the contract by reason of a fraud in prospectus, as the same was not addressed to him.

(n) *Laidlow v. Organ*, 2 Wheat 178.

(o) L.R. 9 Q.B. 531.

(p) 11 Ch.D. 363.

(q) *Molyncux v. Hawtrey* (1903), 2 K.B.

(r) *Venezuela Railway Co. v. Kisch*, L.R.

2 H.L. 113.

(s) *With v. O'Flanagan* (1936), 1 Ch. 575.

(t) (1873), L.R. 6 H.L. 377.

Misrepresentation (sec. 18)

Misrepresentation, according to sec. 18 is of three types : (i) too positive assertion (i.e. in a manner not warranted by the information of the person making it) of that which is not true, though he believes it to be true ; (ii) any breach of duty, which without intention to deceive, gains an advantage to the person committing it, by misleading another to his prejudice ; (iii) innocently causing a party to the agreement to make a mistake as to the substance of the agreement.

Fraud and Misrepresentation distinguished

This attempt to classify various cases of misrepresentation, makes the distinction between it and fraud very clear : (i) both consist of a false statement but while in fraud, the false statement is made with the knowledge that it is false or at least without any belief in its truth, in misrepresentation, the party believes in the truth of the statement which he makes. In other words, misrepresentation may be either (a) fraudulent, in which case it falls under sec. 17, or (b) innocent, in which case it falls under sec. 18. The other point of difference may be stated thus : (ii) fraud or deceit is a tort, i.e. a civil wrong, which, independently of any contract, entitles a party to claim damages. Misrepresentation, however, is not a tort and no damages can be claimed for negligent misrepresentation. (iii) In case of misrepresentation, the fact that the party misled had the means to discover the truth with ordinary diligence will prevent the party from avoiding the contract ; this is never so in case of fraud, except in the case of fraudulent silence.

Misrepresentation explained

Cl. (1) of sec. 18 refers to a class of cases of which *Mohanlal v. Shri Gangaji Cotton Mills (u)* is an instance. In this case A's statement to B that C will be a director of a company, made by him from purely hearsay information, was held to entitle B to avoid the contract to take shares under the sec., the statement being false. Cl. (2) was invoked in *Oriental Banking Co.'s case (v)*. It is intended to cover the class of cases, which go under the name of "constructive fraud" in England. Cl. (3) was brought into play, where a Bank was induced to discount a bill of exchange drawn by a company under the signature of two of its directors and the secretaries, treasurers and agents, when the articles required three directors to sign a bill in order to bind the company. The Court held that the company innocently represented to the Bank that the bill was valid and operative and that therefore the case fell under cl. (3) of the sec. (w). Notice that the mistake required here is as to the substance or a material part of the contract. In *Redgrave v. Hurd (x)* R had induced H to purchase his business as a solicitor by a mis-statement of its value. It was found that the statement was not false to R's knowledge and that R had no intention to deceive. Held, H was entitled to avoid the contract. Parties can, by mutual agreement, make any term or terms material. Notice that, as held by the Privy Council in *Pratap Chandra v. Mahendra (y)*, misrepresentation may be of fact as well as of law.

(u) 4 C.W.N. 369.

(v) P. 20 (supra).

(w) Re Nursey Spinning and Weaving Co.,

5 Bom. 92.

(x) 20 Ch.D. 1.

(y) 16 I.A. 233.

Consequences of Coercion, Fraud, etc. (secs. 19, 19A)

Sec. 19 provides that where consent to an agreement is caused by coercion, fraud or misrepresentation as defined by the previous secs., (i) the contract is voidable at the option of the party whose consent was so caused. (ii) Where consent has been caused by fraud or misrepresentation, the party misled may, if he so chooses, insist that the contract shall be performed by the other party as agreed, and that he be put in the same position as he would have been, if the representation made were true. To the above rule of voidability, however, there are certain exceptions, viz. (i) where consent has been caused by "misrepresentation" (sec. 18) or (ii) by silence "fraudulent" within the meaning of sec. 17, the contract shall not be voidable, if the party misled had the means of discovering the truth with ordinary diligence. (iii) If the fraud or misrepresentation which has been used, did not cause the party to give his consent, the contract is not voidable at the instance of that party. In other words, the sec. gives two rights to a person whose consent to a contract has been caused by fraud or misrepresentation: (i) he can either, avoid the contract or (ii) affirm the contract and require the other party to carry it out as agreed.

Thus if A induces B to advance Rs. 10,000 to A on the security of his property, fraudulently representing to B that the property is unencumbered, B can, on discovering the fraud, either avoid the contract and call upon A to refund the amount forthwith to him or, at B's option, require A to redeem the prior encumbrance and give him the property free from the mortgage as agreed. In the last case, A cannot be heard to say that he was not bound by the contract, because to do so, would be to allow A to take advantage of his own fraud.

Exceptions to right of rescission

The right to avoid, i.e. to rescind the contract, which is given by the sec. in the two cases of fraud and misrepresentation is subject to certain exceptions. These are (i) in case of innocent misrepresentation (sec. 18), the party misled thereby has no right to avoid the contract, if he could have discovered the truth by using ordinary diligence. (ii) In case of fraudulent silence as defined by sec. 17, the party misled has no right to rescind the contract if he could have discovered the truth by the use of ordinary diligence. This exception impliedly makes it clear that in other cases of fraud as defined by sec. 17, e.g. "fraudulent misrepresentation", the fact that the party misled has means of discovering the truth by the use of ordinary diligence is no ground to prevent the exercise of the right of rescission given by the sec. (iii) In cases where fraud or misrepresentation has been practised, the party will not be allowed to avoid the contract on that ground, if such fraud or misrepresentation has not been the cause of the party entering into the contract.

In *Horsfall v. Thomas* (2), a defective cannon which was the subject of sale, was plugged by the vendor in order to conceal the defect from the prospective purchaser. The latter, however, never inspected the cannon. *Held*, the contract could not be avoided on the ground of fraud.

To the above exceptions laid down by sec. 19, the following may be added: (iv) If after becoming aware of the fraud or misrepresentation, the party misled, either by express words or by an unequivocal act, shows an intention to affirm the contract, the right of rescission will be gone (a). (v) If before the contract is avoided third parties, *bona fide* and for value,

(2) 1 H. & C. 9.

(a) *Clough v. L.N.W. Rly.*, L.R. 7 Ex. 26.

acquire interest in the subject-matter of the contract, the right to rescind will no longer be available. This subject is dealt with by secs. 27-30 of the Sale of Goods Act (see seq.). (vi) Before the right to rescind can be exercised, the party entitled to it must be in a position to achieve "*restitutio in integrum*", i.e. restoring the parties in the same position as when the contract was made. If such a thing is not possible, the right cannot be exercised. Thus it has been held that a shareholder who has been induced to take up shares by false statements in a prospectus, cannot avoid the contract after a winding up order has been made (b). He cannot do so, even after a petition for winding up has been filed (c). (vii) It has been held in some cases in England that in case of innocent misrepresentation (sec. 18), the contract cannot be avoided if it has already been executed, e.g. if under a lease, the lessee has already taken possession (d). The rule, however, has been doubted in subsequent cases (e). It has now been held in England that an executed contract of sale of goods can, in a proper case, be rescinded on the ground of innocent misrepresentation (f). But this right might be lost by too long a delay. Thus in a recent English case where a painting was innocently sold as a "Constable", but was found, after five years, not to be a genuine "Constable", held, the plaintiff was not entitled to rescind the contract, though he could sue for damages (g). (viii) The right may also be lost by allowing the limitation period to elapse. See the Limitation Act (seq.).

Remedies in case of fraud and misrepresentation

In both, (i) the party misled has the right to avoid the contract, except in certain cases (see ante). (ii) In cases of fraud, damages can be recovered, but not in case of mere innocent misrepresentation. (iii) Both cases entitle the party misled to resist a suit for specific performance of the contract or for damages for breach of the contract at the instance of the guilty party. (iv) In both cases the party misled, may, if he so chooses, affirm the contract and compel the other party to carry it out as agreed.

Legal consequences of undue influence (sec. 19A)

Sec. 19A provides that where a contract is induced by undue influence, (i) the contract is voidable at the instance of the party dominated upon. (ii) The Court may, at his instance, set aside the contract absolutely or on such terms, as to return of benefits obtained thereunder, as the Court thinks just. Thus, as the illustration shows, if A by undue influence makes B sign a pro-note for Rs. 200 when Rs. 100 only have in fact been advanced, the Court can, while refusing to enforce the promissory note against B, require B to pay back Rs. 100 actually advanced by A.

Mistake (secs. 20-22)

Sec. 20 of the Act provides that "when (i) both parties to an agreement are under a mistake (ii) as to a matter of fact (iii) essential to the agreement, the agreement is void". Three conditions must be satisfied, before a contract can be avoided on the ground of mistake: (i) the mistake must be of both the parties, i.e. mutual and not unilateral; (ii) it must be a

(b) Oakes v. Turquand, 2 H.L. 325.

(c) First National Insurance Co. v. Greenfield (1921), 1 K.B. 260.

(d) Angel v. Jay (1911), 1 K.B. 666.

(e) Armstrong v. Jackson (1917), 2 K.B.

at p. 825.

(f) Solle v. Butcher (1949) 2 All E.R. 1107.

(g) Leaf v. International Galleries (1950) 1 All E.R. 693.

mistake of fact and not of law ; and (iii) it must be about a fact essential to the agreement and not about one which is subsidiary thereto.

To take the above conditions separately, as to (i) sec. 22 makes it quite clear that a contract is not voidable merely because one of the parties was under a mistake of fact relating thereto. In other words, it is only a bilateral mistake which can avoid a contract.

Thus when a charter party provided that the steamer should be available at Jeddah on 10th August 1892, "15 days from Haj", the plaintiff being under the (erroneous) belief that 15 days from Haj commenced with 10th August 1892, while the defendant company was under no such illusion, it was held that the plaintiff had no right to avoid the contract on the ground of mistake, the mistake, if any, being not mutual but of one party only (h). Two points, however, must be noted here : (a) If the mistake is caused by the fraud or misrepresentation of the other party, the contract would be voidable under sec. 19. (b) Under the doctrine of *Smith v. Hughes* (i) if the fact of the unilateral mistake is known to the other party, and the latter party also knows that the first party is consenting because of it, the contract would be voidable. The principle of the rule is stated to be that when one knows that another understands his offer in a different sense from that in which he makes it, the transaction will not be allowed to stand (Anson, p. 162). Thus in *Webster v. Cecil* (j) W offered to C to purchase certain plots of land belonging to C at £2,000. C rejected the offer. Afterwards C wrote a letter offering to sell the plots to W for "£1,200", his real intention being to make an offer for "£2,100". W accepted the offer as made. Held, W was not entitled to enforce the contract, as he knew that the "offer" was made by C under mistake.

Secondly, the mistake must be of fact and not of law. In this connection the explanation to sec. 20 makes it clear that an erroneous opinion of the value of the subject-matter of the contract is not such a mistake of fact. Similarly, sec. 22 lays down that a mistake of foreign law is a mistake of fact and not of law. The rule is based on the maxim "*Ignorantia Juris non excusat*", i.e. ignorance of law is no excuse to avoid a contract. This is because everyone is supposed to know the laws of the State whose subject he is. On the other hand, one cannot be expected to know the laws of a foreign State. A mistake of such law, therefore, is regarded as a mistake of fact.

Thus where in ignorance of the law of India, parties agreed to pay interest on the amount of a decree, where the decree provided for no payment of interest, it was held that no relief could be granted (k). Similarly, where a term in a mortgage deed provided that the mortgagee shall become the owner of the property if the mortgagor failed to redeem within 8 years (the legal period being 60 years), it was held that the agreement was binding (l). A mistake as to the law of registration with regard to a deed of assignment has been recently held by the Supreme Court to be a mistake of law and therefore not capable of avoiding a contract under sec. 21 (m).

Notice in this connection, however, that a mistake as to the existence of a private right is a mistake of fact, though such a right may depend on rules of law. Thus in a Calcutta case a lease was granted by the landlord of certain lands belonging to himself to the plaintiff. Both parties believed at the time that the lease would carry with it mineral rights in the sub-soil. A later decision of the Privy Council threw grave doubts on the proposition. Held, plaintiff was entitled to rescind the contract and ask for a refund of moneys paid by him in advance (n).

(h) *Haji Abdul Rehman v. Bombay Persia Steam Navigation Co.*, 16 Bom. 561.

(i) (1871), 6 Q.B. 597.

(j) 30 Beav. 62.

(k) *Goculdas v. Muli*, 5 I.A. 78.

(l) *Vishnool v. Kashinath*, 11 Bom. 174.

(m) *Kalyanpur Lime Works v. State of Behar* (1954) S.C.J. 99.

(n) *Ramchandrar v. Ganesh*, 21 Cal. W.N. 404.

The third and last condition is that the mistake must be as to a fact essential to the agreement. If it is with regard to a subordinate term of the contract, the contract cannot be avoided.

Thus where a cargo of corn was sold as coming from Salonica to England, but unknown to both the parties, the corn, at the date of the contract, had already been unloaded and sold at Tunis, because of deterioration, it was held that the contract was void by reason of mutual mistake (o). Similarly, where a life policy was assigned but at the date of the assignment, the assured was already dead, though this fact was not known to any of the parties, it was held that the contract could not be enforced (p). In a Calcutta case, a sale of property was set aside, where it was found that unknown to both the parties the property had already been notified for acquisition by the Calcutta Corporation (q).

Where however the mistake is not of the substance of the contract, the contract cannot be set aside under the section.

Thus in *Bell v. Lever Brothers* (r), Lever Brothers sought to set aside an agreement under which they had paid large sums of moneys to the defendants to induce them to retire from the board of directors of a certain company. The plaintiffs subsequently discovered that the defendants had been guilty of several breaches of duty for which they could have been summarily dismissed from the Board, without need of paying any compensation. No concealment by the defendants was proved. It was held by the House of Lords, by a majority, that under the circumstances, there was no mistake as to any essential term of the agreement, and the agreement, therefore, could not be set aside. Similarly, in a Bombay case, it was held that an agreement of lease could not be set aside on the ground that both the parties thereto incorrectly believed that Government assessment with respect thereto will never be increased (s). Observe that, as distinct from the case of fraud, misrepresentation, etc. a contract entered into under mistake, as defined by sec. 20, is void, and not voidable.

Two further points may be noticed here in the above connection. Where a contract is expressly made "subject to all defects", a mistake in any essential term of the contract will not vitiate the same. Thus where a mortgagee assigned all his right, title and interest under the mortgage to another "subject to all defects", and the mortgage subsequently turned out to be inoperative in law, it was held that the sale could not be set aside. Secondly, if a mistake is made, not in the making of the contract but in the expression of it, the contract cannot be set aside. The remedy, in such a case, is rectification, which the Court can grant under the Specific Relief Act. Notice further, that where a contract becomes void or is discovered to be void, any benefit obtained thereunder will have to be returned under sec. 65 of the Act.

Unlawful consideration or object (sec. 23)

One of the conditions of a valid contract is that the consideration or object thereof should be legal (see sec. 10 ante). When consideration or object of an agreement will be regarded as unlawful is laid down by sec. 23. In the following six cases, consideration or object of an agreement is deemed unlawful: (1) if it is forbidden by law; (2) if it is of such nature that, if permitted, it would defeat the provisions of any law; (3) if it is fraudulent or (4) involves injury to the person or property of another or (5) if the Court regards it as immoral or (6) opposed to public policy. In each of the above cases, the contract is void.

(o) *Conturier v. Hastie*, 5 H.L.C. 673.

(p) *Scott v. Coulson* (1903), 2 Ch. 249.

(q) *Nursing Dass v. Chuttoo*, 50 Cal. 615.

(r) (1932), A.C. 161.

(s) *Babshetti v. Venkataraman*, 3 Bom. 154.

Forbidden by Law

Taking the cls. separately, cl. (1) refers to contracts which are declared illegal by Statute, e.g. contracts for sale or purchase above the standard price fixed by Statute with regard to a controlled article. A Statute, however, may not expressly prohibit a contract but may impose penalties on the parties for entering into it. The effect in each case depends upon the proper construction of the language of the Statute. When the language is doubtful, however, English Law has made a distinction which has been followed by Courts in India. If the object of imposing the penalty is merely to protect revenue, a contract in violation of the terms of the Statute is not necessarily illegal. If the object, however, is to protect the general public or a particular class of it, an agreement for which the penalty is imposed will be regarded as forbidden by law and therefore illegal (t).

Following the above principle, it has been held in India that where the holder of a licence for collecting tolls, sub-leased it to another in violation of the terms of the licence (u), and where the licensee of a right to cut grass from a forest, assigned it to another (v), when the licence provided a penalty for doing so, the transactions were not void though they may expose the wrong-doer to the stipulated penalty. On the other hand, a sub-lease of a licence for manufacture and sale of country liquor (under the Abkari Act) (w), of opium (under the Opium Act) (x) or Salt (under the Bombay Salt Act of 1890) (y) was held to be void, as the prohibition imposed by the respective Acts was for the protection of the public and not for mere administrative convenience. Where a business in an article governed by the Abkari Act was sold with an indemnity to the vendor against all losses, it was held that the vendor could not make the purchaser liable on the indemnity (z). A question has arisen whether a partnership in such a case would be within the mischief of the sec. It was held by the Bombay High Court that it would not be; the reason being that such a transaction does not involve any transfer or assignment of the business in question (a). Much, however, depends on the language of the prohibition. Recently it has been held that a loan granted to the guardian of a minor to enable him to celebrate the minor's marriage in contravention of the Child Marriage Restraint Act is illegal and cannot be recovered back (b). Similarly it has been held that a forward contract which offends against the provisions of the Vegetable Oil and Oilcakes (Forward Contracts Prohibition) Order is illegal and void. Damages for breach of such a contract cannot form consideration of any contract (c). In a recent English case a motor car was sold by the plaintiff to the defendant which did not comply with certain requirements of the English Motor Vehicles (Construction and Use) Regulation, 1951. Non-compliance with the Rules was made an offence. Held, the seller could not recover the price, as the contract was tainted with illegality (d). An agreement to pay consideration to a tenant to induce him to vacate premises governed by the Rent Restriction Act is illegal and cannot be enforced (d1). In a recent English case, the plaintiffs and defendant (Indian subject), had agreed that the defendant should sell to the plaintiffs a certain quantity of bags C.I.F. Genoa. To the knowledge of both parties, the goods were to come from India and were required for sale to South Africa. By certain Regulation of the Government of India, taking by sea or land, out of India, goods destined for Union of South Africa was prohibited. The

(t) Anderson v. Daniel (1924), 1 K.B. 138.
 (u) Bhikanbhai v. Hiralal, 24 Bom. 622.
 (v) Nazari v. Babamiya, 40 Bom. 64.
 (w) Debi Pershad v. Rup Ram, 10 All. 577.
 (x) Raghunath v. Nathu, 19 Bom. 626.
 (y) Ishmalji v. Raghunath, 33 Bom. 636.
 (z) Bihari Lal v. Jagadish, 31 Cal. 798.
 (a) Champsi v. Gordhandas, 19 Bom. L.R. 381.

(b) Shrinivas v. Raja Ram Mohan (1951), 2 Mad. L.J. 264.
 (c) Pottimurthi v. Tadepalli, A.I.R. (1953) Mad. 845.
 (d) Vinall v. Howard (1953), 2 All E.R. 515, reversed on another point (1954), 1 Q.B. 375.
 (d1) Mohanchana v. Manindra, A.I.R. (1955) Cal. 442.

defendant failed to ship the goods. *Held*, the contract was illegal, and could not be enforced by the plaintiffs (*d2*).

Defeat the provisions of Law

Cl. (2) refers to cases where, there being no express statutory prohibition against a particular type of contract, the nature of the contract is such that it would be against the spirit of a particular law, whether enacted or otherwise.

Thus an undischarged insolvent, privately settling with a creditor, on condition that he would not oppose discharge has been held to be covered by the cl. (*e*). Similarly, a collusive assignment of the benefit of a contract by a person to his brother-in-law, on the eve of the former's insolvency has been held void. This is because, such transactions violate the basic principles of Insolvency Law (*f*). An agreement in violation of the Rent Act is also void (*g*). Similarly, an agreement to give an annuity to the father and mother of an adopted Hindu boy, in order to induce them to consent to the adoption has been held void, because of a text of Hindu Law which lays down that a son should be affectionately given in adoption (*h*). An agreement between a Mahomedan husband and wife that the latter, after marriage, shall reside with her parents, was held to be void as being against the principles of Mahomedan Law of Marriage (*i*). Apart from these cases an agreement may be void as being against general principles of law. Thus an agreement between parties that a will shall not be contested and that probate should issue in favour of a specified person is bad, as it excludes evidence in proof of a will, which by law is a public document (*j*).

Fraudulent (Cl. 3)

This cl. refers to contracts which are entered into to promote a fraud. Thus an agreement between several persons to purchase shares for the purpose of inducing the public to believe that there was a market for the shares and that the shares were being sold at a real premium was held to be illegal and no action could lie on a purchase effected under such conditions (*k*). Similarly, in India, an agreement between two persons to cheat the Commissariat Department, by submitting a tender in the name of one of them only, though they were both partners in the transaction, has been held to be void (*l*).

Injury to person or property (Cl. 4)

This refers to acts of criminal violence. Thus an agreement to commit an assault is void (*m*). Similarly, it has been held that an insurance policy cannot be enforced when the assured has feloniously committed suicide (*n*).

Immoral (Cl. 5)

This refers to contracts which offend against principles of morality. Thus rent due in respect of premises let to a prostitute to enable her to carry on her trade cannot be recovered (*o*). A loan to such a person for

(*d2*) *Regezone v. Sethia* (1956) 1 All E.R. 229.

(*c*) *Nairoji v. Kazi Siddic*, 20 Bom. 636.

(*f*) *Jaffri Meherali v. Budge Budge Jute Mills*, 34 Cal. 289.

(*g*) *Salch v. Manekji*, 50 Cal. 491.

(*h*) *Eshan Kishore v. Harish Chandra*, 13 B.L.R. App. 42.

(*i*) *Abdul v. Husseni*, 6 Bom. L.R. 602.

(*j*) *Manmohini v. Banga Chandra*, 31 Cal. 357.

(*k*) *Scott v. Brown* (1892), 2 Q.B. 724.

(*l*) *Sibram v. Nagarmal* (1884), Panj. Recs. No. 63.

(*m*) *Allen v. Rescous*, 2 Lev. 174.

(*n*) *Beresford v. Royal Insurance Co.* (1938), A.C. 586.

(*o*) *Sultan v. Nanu* (1877), Panj. Recs. No. 22.

the same purpose is also unrecoverable (p). An assignment of a mortgage to a woman in consideration of future cohabitation has been held illegal (q). A question has arisen as to whether arrears of allowance for past cohabitation can be recovered. The Allahabad High Court has held that there is no objection to its recovery (r). All the other High Courts however have held otherwise (s). In England it has been held that an agreement between a married man and a woman who knows that the former is married, for future marriage after the death of the first wife is void as being immoral (t).

Public policy (Cl. 6)

Public policy in a term of very wide connotation. The phrase, however, is used here in a technical sense, as meaning, opposed to the policy of law, and is restricted to certain fixed heads, the rulings of the highest Courts in England being that its meaning as so restricted will not generally be extended beyond the recognised class of cases (u). It has been held to include the following types of agreements: (i) agreements which tend to injure the State in its relations to other States (e.g. trading with the enemy); (ii) agreements which tend to pervert the due course of justice (e.g. stifling prosecutions, champerty and maintenance); (iii) agreements tending to injure public services (e.g. sales of public offices and pensions); (iv) agreements which are opposed to good morals (see ante); (v) agreements interfering with freedom of marriage (e.g. restraint of marriage, marriage brokerage contracts, etc.); (vi) agreements in restraint of trade; (vii) agreements creating interest against duty. Of these, some types of contracts form the subject of separate secs. in the Contract Act, e.g. agreements in restraint of marriage (sec. 26) and those in restraint of trade (sec. 27).

Trading with Alien Enemy

Taking the remaining cases, separately, (i) refers to trading with an alien enemy. An "alien enemy" according to English Law means a person owing allegiance to a Government at war with the King. Trading with such person without the King's licence is bad.

Thus a policy of insurance taken out with respect to enemy goods cannot be enforced (v). Similarly, an agreement to ship cargo from an enemy port, even in a neutral vessel, is void (w). Note in this connection that the test of enemy status is not nationality but the place where the person voluntarily resides or carries on business (x). Thus a British or a neutral subject carrying on business in an enemy country may be an enemy (y).

The rules with regard to an alien enemy according to English Law are that (i) he cannot, during the continuance of the war, enter into contracts with a British subject; (ii) he cannot, until the war is over, sue in British Courts, except with leave. (iii) Contracts entered into before war between British subject and another who subsequently becomes an alien enemy, are on declaration of war, dissolved, (a) if the contract involves intercourse

(p) *Bholi Bakshi v. Gulia* (1876), Panj. Recs. No. 64.

(q) *Thasi v. Shanmugvelu*, 28 Mad. 413.

(r) *Dhiraj Koer v. Bikramsing*, 3 All. 387.

(s) *Hussenalil v. Dinbai*, 25 Bom. L.R. 552.

(t) *Wilson v. Carnley* (1908), 1 K.B. 740.

(u) *Jenson v. Driefontain Consolidated Mines* (1902), A.C. 484.

(v) *Jenson v. Driefontain Consolidated Mines* (Supra).

(w) *Potts v. Bell* (1800), 8 T.R. 548.

(x) *Porter v. Freudenberg* (1915), 1 K.B. 857.

(y) *Screfract v. Udens* (1943), A.C. 203.

with an alien enemy, e.g. partnerships (z) or (b) if the continued existence of the contract would be contrary to public policy, e.g. contracts the performance of which would be of assistance to the enemy State (a). (c) Similarly, if the nature of the contract is such that performance of the contract after the termination of the war would be of an entirely different character than what the parties intended it to be when the contract was entered into, the contract will stand dissolved on the outbreak of war, e.g. contracts of charter party and affreightment, contracts of service, etc. (b). Contracts which do not fall under the above groups are held to be suspended during war, with a possibility of their revival on its termination, e.g. a shareholder's contract with a company (c), an insurance policy (d), a lease of property (e). Notice in this connection that an agreement to promote hostile action in a friendly State is also void as being opposed to public policy (f).

Stifling prosecutions

The principle of law is that you shall not make a trade of a felony (g). A person, therefore, cannot compromise a public offence for reward. In India, however, the Criminal Procedure Code divides offences into (i) compoundable and (ii) non-compoundable offences. Withdrawing or agreeing to withdraw a prosecution for a compoundable offence is not objectionable, e.g. assault. Where, however, the offence is non-compoundable, e.g. criminal breach of trust, an agreement to withdraw a prosecution for such offence in consideration of the accused passing a bond for the sum misappropriated cannot be enforced (h). It has been recently held in Bombay that a mere threat to prosecute is not enough. An agreement not to prosecute or to continue a prosecution must also exist as part of consideration for the contract before the latter can be avoided as being against public policy (i).

Champerty and maintenance

Maintenance means "an agreement to promote litigation in which one has no interest of his own". Such agreements are absolutely void in English Law as tending to stir up litigation and therefore as being against the policy of law. Champerty means "an agreement whereby one party promises to assist another in recovering property by suit in consideration of his receiving a share in the property if recovered". Such agreements are also absolutely void in English Law for the same reason. In India, however, a different rule has been applied since 1874. This is because of the peculiar condition of the Indian people, who are proverbially too poor to secure even one square meal a day. The rule applied in India, therefore, is that an agreement by way of maintenance or champerty is not necessarily void, unless there are elements of moral turpitude or unconscionable conduct proved in connection therewith (j).

Thus a transfer of property which is the subject of litigation and which is in the possession of the defendant has been held to be valid (k). Similarly, where payment

(z) *Stevenson v. Akt. Fur. Cartonagen Industrie* (1918), A.C. 239.

(a) *Zink Corporation v. Hirsch* (1916), 1 K.B. 541.

(b) *Esposito v. Bowden*, 7 El. & Bl. 763.

(c) *Ertal v. Rio Tinto* (1918), A.C. 269.

(d) *Seligman v. Eagle Insurance Co.* (1917) 1 Ch. 519.

(e) *Hainley v. Lowenfield* (1916), 2 K.B. 707.

(f) *De Wutz v. Hendricks*, 2 Bing. 316.

(g) *Lord Westbury in Williams v. Bayley* L.R. 1 H.L. 200.

(h) *Amir Khan v. Amir Jan*, 3 C.W.N. 5.

(i) *Ramchandra v. Bank of Kolhapur*, 54 Bom. L.R. 245.

(j) *Ramkomar v. Chander Kanto Mukerji*, 4 I.A. 23.

(k) *Achal Ram v. Kazim Hussain*, 32 I.A. 113.

of consideration was made dependant on the transferee's success in a litigation, the agreement was held not to be void (l). An agreement to share the subject of litigation has also been upheld in India (m). Again, where the reversioners of a Hindu widow, who had alienated her husband's properties of the value of Rs. 3 lakhs, assigned their right to have the alienation set aside for Rs. 5,200, out of which only Rs. 600 were paid down, the Privy Council held that the transaction could not be set aside, the test being the commercial value of the subject-matter of the contract at the date of the transaction (n). On the other hand, if the whole object appears to be to gamble in litigation, or if the terms are too extortionate, the transaction will be set aside. Thus where a liquidator of a company, having compromised a claim of Rs. 3 lakhs against a contributory, on the assurances of his friends that he could not pay more, assigned the claim, ten years after, to an entire stranger, who sued to set aside the transaction as fraudulent, it was held that the object being merely to traffic in litigation, the suit must be dismissed (o). Legal practitioners' contracts with their clients, to share in the subject of the litigation, if the client succeeds therein, are void, under the Legal Practitioners' Act. Bribing a judge to induce him to decide in a party's favour is also against public policy.

Interference with public offices

This class includes contracts for the sale of public offices, e.g. assignments of salaries and pensions attached to such offices. This is because the public is entitled to be served by the fittest persons procurable and because such persons should not be exposed to temptations by poverty or otherwise. Thus the office of a Receiver or Official Trustee cannot be assigned nor that of a Mutawalli (p) of a mosque. Similarly an agreement to make a donation to charity in consideration of a promise to secure a Knighthood has been held to be void (q).

Marriage brokerage contracts

These are contracts made in consideration of procuring or bringing about a marriage. They are illegal as tending to pervert the social institution of marriage, which should always be based on free choice of the parties concerned (r). In England such contracts are always bad. In India, however, different conditions prevail and marriages are generally brought about by parents. It has been held in India, however, that an agreement to pay money to the parent or guardian of a minor in consideration of his consenting to give the minor in marriage is void (s). If, therefore, the minor is ultimately not given in marriage, the plaintiff cannot recover damages (t). Similarly, the parents cannot recover the promised reward, on the marriage being brought about (u). An agreement to pay money to procure a wife has also been held to be void (v).

Interest against duty

This class covers cases of agreements with public servants to use their influence with other public servants to procure some benefit for another.

(l) Bhagwat Dayal v. Debi Dayal, 35 I.A.

48. (m) Kunwar Ram v. Nilkantha, 20 I.A.

112. (n) Bhagwat Dayal v. Debi Dayal (Supra).

(o) Goculdas v. Lakhmidas, 3 Bom. 402.

(p) Wahidali v. Ashruff, 8 Cal. 732.

(q) Parkinson v. College Ambulance (1925), 2 K.B. 1.

(r) Herman v. Charlesworth (1905), 2 K.B. 131.

(s) Dholidas v. Fulchand, 22 Bom. 658.

(t) Ibid.

(u) Baldeo Das v. Mohamaya, 15 Cal. W.N. 447.

(v) Vaithyanathan v. Gangarazu, 17 Mad. 9.

Such agreements are void. An agent dealing on his own account in the business of agency without the knowledge of his principal (secs. 215-16) also falls within this clause.

VOID CONTRACTS

Contracts declared to be void (secs. 24-30): The last condition of a valid contract as defined by sec. 10 is that it must not be one which is declared to be void by the Act. The agreements which are declared to be void by secs. 24-30 are : (i) agreements, part of the consideration or object of which is illegal (sec. 24); (ii) agreements without any consideration (sec. 25); (iii) agreements in restraint of marriage (sec. 26) or (iv) in restraint of trade (sec. 27); (v) or of legal proceedings (sec. 28); (vi) uncertain agreements (sec. 29), and (vii) agreements by way of wager (sec. 30). To these may be added (viii) agreements to do an impossible act (sec. 56); (ix) a minor's agreement (see ante) and (x) agreements induced by material mistake of fact (sec. 20).

Part of consideration or object unlawful (sec. 24)

Under sec. 24 where part of a single consideration for one or several objects or where any one or any part of any one of several considerations for a single object is void, the whole agreement is void. The sec. refers to agreements in which a part of the consideration or object being illegal, it cannot be separated from the other part which is valid and effective. In such a case, the whole agreement is void.

Thus where a pro-note was passed for a sum which included amounts due in respect of lotteries (w) and gambling losses (x) the whole was held void. Similarly, an agreement to pay Rs. 50 per month to a married woman for living in adultery and also for acting as house-keeper was held to be totally unenforceable (y). If, however, the promises are severable the Court will enforce the valid part of the agreement (z).

Agreements without consideration (sec. 25)

Sec. 25 lays down that an agreement made without consideration is void, consideration being an essential part of a valid contract as explained before. The sec. however lays down certain statutory *exceptions* to the above rule, where there being in fact no "consideration" as defined by law, the agreement is still regarded as valid and operative in law. These exceptions are as follows :

(1) A contract (i) in writing, (ii) registered, (iii) on account of natural love and affection, (iv) between parties standing in a near relation to each other, is valid, though there is no consideration to support it. This exception to be operative requires all the above four conditions to be fulfilled.

Thus a husband and a wife, a father and son, a brother and a brother are persons standing in a near relation, but others may not be. Where a brother gratuitously undertook to discharge the debts of his other brother and all the other requirements of the clause were satisfied, it was held that the latter could sue the former in the event of his not carrying out the agreement (a). Similarly, natural love and affection should be the motivating cause before the clause can apply. Thus where an agreement for separate maintenance was arrived at between a husband and a wife but the cause was

(w) Joseph v. Solano, 9 B.L.R. 441.

(x) Balgovind v. Bhagu, 35 All. 558.

(y) Alice v. William Clark, 27 All. 266.

(z) Putnam v. Taylor (1927), 1 K.B. 639.

(a) Venkatasamy v. Rangasami, 6 Mad. 71.

constant quarrels between the two, it was held that the clause could not be invoked (b). The agreement must also be registered.

(2) A promise to compensate, wholly or in part, a person who has voluntarily done something for the promisor, or something which the promisor was legally compellable to do is also good, without consideration. Notice that the exemption does not require either writing or registration. Past services being good consideration under sec. 2, cl. (a), if rendered at the desire of the promisor, this clause provides for cases where such services have been rendered without any request proceeding from the promisor. A promise to pay for past services voluntarily rendered, therefore, is not valid as a "contract" but is enforceable in law by reason of the statutory exception created in its favour by cl. (2) of sec. 25. Before the exception can apply, however, it is essential that (i) the promisor should be in existence at the time the service is rendered. Thus a promoter's services on behalf of a company to be formed, cannot form the subject of a subsequent promise by the company to pay for them because there was then no company in existence (c). (ii) The promisor must also be competent to contract. Thus services rendered voluntarily to a person during his minority will not support a promise made after attaining majority to pay for them (d). (iii) The act done must also be legal. Thus past cohabitation will not make a promise to pay for it enforceable under this clause (e).

(3) Where a promise (i) in writing (ii) signed by the person making it or by his authorised agent, is made to pay a debt barred by limitation it is valid without consideration. A time-barred debt is not recoverable at law and therefore can form no consideration for a promise; hence the importance of the present exception. Before the exception can apply, however, it is necessary that there should be a *promise* to pay as distinguished from a mere "acknowledgment of liability" in respect of the debt. For such acknowledgment to be effective, it should be made before the debt is time-barred (see sec. 19, Limitation Act). If, therefore, what is given is an "acknowledgment" only and not a "promise" to pay, the clause will not come into operation.

In this connection it has been held that opening a "khata" is merely an acknowledgment of liability (f); so too a bare statement of account signed by the debtor in favour of the creditor (g). Where the words "Bakideva" ("due and payable") appeared at the foot of a "khata" in the handwriting and under the signature of the debtor, the result was also the same (h). Where, however, a "khata" signed by the debtor said "Rs. 200 are found due on previous account being made up. For the same this 'khata' is passed. Moneys are payable by me. I am to pay the same whenever you make a demand", it was held that there was a sufficient promise to satisfy the clause (i). Notice that a promise to pay a time-barred debt due by a third person, is not within the exception.

English Law recognises at least two further exceptions to the general rule that contracts not supported by consideration are void, which may be mentioned here: (1) Contracts under seal are valid according to English Law though not supported by consideration. They are also known as "specialty contracts". The deed must be in writing or printed on paper or

(b) Rajlakhi Devi v. Bhutnath, 4 C.W.N. 488.

(c) Ahmedabad Jubilee Co. v. Chhotalal, 10 Bom. L.R. 141.

(d) Indran v. Anthappa, 16 Mad. L.J. 422.

(e) Husseinali v. Dinbai, 25 Bom. L.R. 252.

(f) Chawksi Himatlal v. Achratlal, 8 Bom.

194.

(g) Ramji v. Dharma, 6 Bom. 683.

(h) Ranchoddas v. Jaychand, 8 Bom. 405.

(i) Chandraprasad v. Varajlal, 8 Bom. L.R. 644.

parchment and it must be "signed, sealed and delivered" in order to be effective in law. Because of their special form, these contracts are valid in English Law without any consideration to support them. There is no counterpart to this kind of contract in Indian Law, where all contracts, whatever their nature or form, require consideration in order to be valid.

(2) The second exception, which is well recognised by Indian Law also, is in case of negotiable instruments, where there is usually no consideration between remote parties, e.g. acceptor and payee. Similarly, an endorsee can have recourse to the drawer, on a bill being dishonoured, though no consideration has passed between the two. Again in case of accommodation bill, the accommodating party, i.e. the acceptor, is liable to the holder thereof, though he has not received any consideration for the bill. These rules are the product of the "Law Merchant" and are justifiable on the footing of the special rules applicable to negotiable instruments as such. Agency and bailment are sometimes described as further exceptions to the above rule. This, however, is not correct, a gratuitous bailment and a gratuitous agency creating only certain specified legal relations between the parties concerned but not by any means a contract. Notice that as the explanations to the sec. show, inadequacy of consideration is no bar to the validity of a contract, though that fact may be taken into consideration by the Court in considering whether consent was freely given. Similarly, a gift (which is not a contract) does not require consideration in order to be valid.

Restraint of Marriage (sec. 26)

Under sec. 26 every agreement in restraint of the marriage of any person, other than a minor is void. This sec. places a prohibition on all forms of restraint on marriage whether partial or complete. Thus under the sec. a contract limited to not marrying a certain person or a certain class of persons will be void. This is not so in English Law, where a restraint on marriage is void only if it is absolute, e.g. agreement to marry no one but the promisee (j). An agreement restraining the marriage of a minor, however, is valid under the sec.

Restraint of Trade (sec. 27)

Under sec. 27 every agreement by which anyone is restrained from exercising a lawful profession, trade or business of any kind, is to that extent, void. The sec. makes every agreement in restraint of trade, whether the restraint is absolute or partial, void. This certainly differs from English Law, which, as it now stands, though making all restraint of trade invalid, does make exceptions in cases where special circumstances justify some kind of restraint being placed on one's liberty of trade (k).

A restraint according to English Law is justified, if it is reasonable (a) having regard to the interest of the contracting parties and (b) the interest of the public (l). Thus a contract against competition entered into by the seller of a business, if confined to the area within which competition would injure the seller's business, has been upheld, while a covenant against any competition at all, has been held to be invalid (m). In the leading case of *Maxim Nordenfelt and Co. v. Nordenfelt* (n) a covenant by Nordenfelt who sold his business to the company, not to carry on any competing business was held to be too wide, both as regards time and space and therefore void. On the other hand, a covenant by him not to carry on for twenty-five years, the manufacture of guns, gun-carriage and ammunition of the kind he was selling to the company, was held valid

(j) *Low v. Pearce*, 4 Burr. 225.

(k) *Morris v. Sexelby* (1916), 1 K.B. 688.

(l) *Wyatt v. Krieger* (1933), 1 K.B. 806.

(m) *Vancouver Malt Ltd. v. Vancouver Breweries Ltd.* (1934), A.C. 181.

(n) 1894 A.C. 515.

as being reasonable under the circumstances. A covenant by an employee not to compete with his employer after termination of service is bad according to English Law (o), though a covenant restraining him from disclosing a trade secret is not (o).

In India, however, the strict language of the sec. has been followed. Thus in a Calcutta case, where a firm of brazier makers contracted with their rivals in the business not to carry on the trade in that particular quarter, in consideration of the latter agreeing to pay off the arrears of pay to their workmen, it was held, on the plaintiffs suspending their business, that the plaintiffs could not enforce the promise against their rivals, the whole contract being in restraint of trade and therefore void under the sec. (p). Similarly, a covenant not to cultivate tea within 40 miles for 5 years after termination of a service agreement was held to be bad (q). Notice, however, that a contract of service is not void under the sec. because of an undertaking by the employee not to serve elsewhere during the continuance of the employment (r). Similarly, ordinary business agreements, e.g. to purchase all requirements from a certain firm or to sell all produce to a certain party, are not void as being in restraint of trade, because they promote business and do not restrain it (s). On the same footing, a pool agreement between manufacturers of a certain article, e.g. ice, to regulate prices and to avoid unnecessary competition between the members has been upheld (t). Such an agreement does not absolutely prevent anybody from carrying on a business but only provides that the business shall be carried on in a certain way.

Three real exceptions to the rule laid down by the sec., however, are recognised by Indian Law. They are: (i) on the sale of the goodwill of a business, the seller may agree not to carry on similar business within specified local limits so long as the buyer carries on like business therein, provided the limits are reasonable in point of time and space [Exc. (1) to sec. 28]. "Goodwill" has been defined as "the advantage or benefit which is acquired by a business, beyond the mere value of the capital, stock, funds or property employed therein, in consequence of the general public patronage and encouragement which it receives from constant or habitual customers". (ii) Similarly, persons entering into a partnership may agree not to carry on a competing business during the continuance of the partnership (see sec. 11, Partnership Act). (iii) Similarly, on a dissolution of a partnership firm, some or all the partners may agree not to carry on the same business, provided in the last two cases, the limitation is reasonable both in point of time as well as space (sec. 36, Partnership Act).

Notice that the sec. does not make the whole agreement void, but void only to the extent that it is opposed to the policy of the law. This would appear to give discretion to the Court to separate the good from the bad part of the covenant.

Thus in an English case (u) where a vendor of a business had covenanted not to deal in "real or imitation jewellery" in the United Kingdom and a number of specified foreign countries though the plaintiff's business was of imitation jewellery only, the words "real or" were deleted by the Court, and the area too was cut down. The matter,

(o) *Morris v. Sexelby* (Supra).

(p) *Madhub Chandra v. Rajkumar Das*,
14 B.L.R. 76.

(q) *Brahmaputra Tea Co. v. Scarth*, 11
Cal. 545.

(r) *Charlesworth v. Macdonald*, 28 Bom.
103.

(s) *Mackenzie v. Streramiyah*, 3 Mad. 472.

(t) *Fraser v. Bombay Ice Manufacturing
Co.*, 29 Bom. 109.

(u) *Goldson v. Goldman* (1915), 1 Ch. 292.

however, cannot be said to be free from doubt. Agreements creating monopolies, with a view to enhance prices to unreasonable extent, would also be void under the sec. (v).

Restraint of Legal proceedings (sec. 28)

Under sec. 28 every agreement by which a party is restrained absolutely (i) from enforcing his rights under or in respect of a contract, by the usual legal proceedings or (ii) which limits the time within which he can enforce his right, is void to that extent. The sec. provides for liberty of legal proceedings as the previous sec. provided for liberty of trade; the principle being that nobody should be restrained absolutely from enforcing his legal rights in a Court of Law.

Thus a term in a contract that no legal action shall be brought thereon is void (w). Similarly, an agreement providing that any dispute between the parties should be settled by arbitration and that neither party should enforce his rights thereunder in Court of Law, was held good as regards the first part but void as regards the second (x). Notice that the sec. refers to absolute restraint. Thus an agreement not to appeal, is not within the sec. (y). An agreement limiting time within which a suit should be brought is void, under the second part of the sec. Thus where an insurance policy provided that no suit shall be brought against the company in connection with the policy, later than one year after the cause of action accrued, it was held that, the clause was void under the sec. (z). Where, however, a policy provided that if no suit was commenced within three months of the rejection of the claim thereunder, all benefits under the policy will be forfeited, it was held that the clause was valid, as nobody was thereby restrained from filing a suit in a Court of Law (a). Notice that a contract extending the period of limitation is bad, not under this sec. but under sec. 23 as being opposed to public policy.

Two exceptions to the rule laid down by the sec. are, however, recognised: (i) an agreement to refer all future disputes in connection with a contract to arbitration [Exc. (1)]; (ii) an agreement to refer all present disputes with regard to a contract to arbitration [Exc. (2)]. The reason for making the exception in favour of arbitration is two-fold: (i) an arbitration agreement does not necessarily oust the jurisdiction of the Law Courts. An arbitrator's award can be set aside and the arbitration proceedings can also be superseded for sufficient cause under the Arbitration Act of 1940 (see seq.). Secondly, an arbitration clause does not prevent a suit being filed in the ordinary Courts with regard to the agreement. It only gives an option to the other party, if he so wishes, to have the suit stayed by an injunction under the Specific Relief Act, an option which that party may or may not exercise.

Uncertain Agreement (sec. 29)

An agreement, the meaning of which is not certain or capable of being made certain is void under sec. 29. Law requires parties to make their own contract. If the words used by the parties are vague or indefinite, the Law cannot lend its help to the parties.

Thus where a motor lorry was agreed to be bought on the basis of price being on the "usual hire purchase terms", the Court held the contract unenforceable, as there were at least three types of "hire purchase terms" known to law, and it was impossible to say which was meant (b). Similarly, where goods were sold "subject to war clause",

(v) *Att. G. of Australia v. Adelaide S. S. Co.* (1913), A.C. 796.

(w) *Coringa Oil Co. v. Koegler*, 1 Cal. 466.

(x) *Ibid.*

(y) *Munshi Amir Ali v. Maharana Indra-*

jit, 9 B.L.R. 460.

(z) *Baroda S. & W. Co. Ltd. v. Satyanarayana etc. Ins. Co.*, 38 Bom. 344.

(a) *Ibid.*

(b) *Scamell v. Ouston* (1941), A.C. 251.

the same result followed, as none could say what was intended (c). An agreement to grant a lease with the addition that "the lease will contain all the usual clauses of a lease of this nature", has been held void for uncertainty (c1).

An agreement of sale "subject to force majeure" is not invalid on the ground of uncertainty; but where the words of a contract were that it was "subject to force majeure conditions" and there were various such conditions known in the trade, *held*, the contract was unenforceable on the ground of uncertainty (d).

Notice, however, that where there is a latent ambiguity in the terms of a contract, it can be cured by extrinsic evidence. Thus in *Burgess v. Wickham* (e), a question arose as to the meaning of the term "seaworthiness" used in connection with a ship called "the Ganges", which having been first used for river navigation, was subsequently put on an ocean voyage, which the Insurance Co. had underwritten. Both parties contended for a different meaning of the word. *Held*, extrinsic evidence was admissible to show the nature of the subject-matter of the contract, e.g. the ship, to which the term was sought to be applied. If the ambiguity is patent, however, no such evidence can be led. Thus where a Bill of Exchange was drawn for "two hundred pounds", but in figures stated for £245, no extrinsic evidence of intention was held to be admissible (f). Notice that where a contract contains terms, which are partly printed and partly written or typed, the latter will prevail over the former in case of conflict (g). An agreement to enter into an agreement is not a contract if an important term of the contract has been left to be settled in the future (h).

Wager (sec. 30)

An agreement by way of wager is void, with certain exceptions. 'Wager' means a bet. A bet can be laid on anything under the sun. The most common case is of horse racing. Two persons lay a bet on horse X, the odds being 8 to 2. This means that there are 8 chances for the horse coming first in the race against 2 of his not coming first. If Rs. 10 have been placed by A and B on the horse in question, A may have to pay Rs. 10 to B in the event of the horse coming first, in return of B having to pay Rs. 2 to A in the event of the horse not coming first. A wager, therefore, is a "game of chance, in which the event, of either gain or loss, is wholly dependent on an uncertain event". From a legal point of view, a wager may be described as "a promise to give money or moneys worth upon the determination or ascertainment of an uncertain event" (Anson). It is in fact a type of contingent contract, the determination of an uncertain event being the sole condition of the fixing of liability under the contract (i). In this sense a wagering contract resembles a conditional promise, a contract of guarantee or a policy of insurance, each of which are contracts of a contingent nature, the happening or not happening of the contingency being the sole test of liability. A contract of guarantee, or a policy of insurance, however, are valid and binding in law, whereas an agreement by way of wager is declared void by the sec. The difference between the two lies in

(c) *Bishop & Baxter v. Anglo Eastern Trading Co.* (1943), 3 A.E.R. 598.

(c1) *Baij Nath v. Kshetrahari*, A.I.R. (1955) Cal. 210.

(d) *British Industries v. Patley Pressings* (1953), 1 All E.R. 94.

(e) 1 B. & S. 669.

(f) *Saunderson v. Piper*, 5 Bing. N.C. 425.

(g) *Noorbhai v. Allabux*, 19 Bom. L.R. 845.

(h) *Loftus v. Roberts* (1902), 18 T.L.R. 532.

(i) *Ironmonger v. Dyne*, 44 T.L.R. 497.

the fact that while in the case of the former type of contract, the parties concerned have an interest of their own to protect and have, for that very reason, entered into the contract in question, the parties in the second case have no other interest therein except the winning or losing of the wager or bet laid between them. An insurance policy taken out by A on his life is valid, because he is interested in protecting his dependents from the consequences of his premature death. In case of betting on a horse, neither of the two parties has anything to lose or gain by the particular horse coming first or last. They lay the bet on the horse, exclusively because, they can thereby make some easy money. This is precisely the reason why wagering contracts are prohibited by law, because they tend to encourage sloth and indolence on the part of the public whereas the policy of the law is the same as that preached by the Bible, viz. "that thou shalt earn thy daily bread in the sweat of thy brow". Obvious instances of wagering contracts are betting on horse racing, purchasing lottery tickets, transactions known as "Ank Farack", i.e. betting on what the particular difference in the forward rates of New York cotton would be at a stipulated time. These are pure gambling transactions and therefore void in law as wagers.

Wagering and speculation distinguished: Wagering or gambling transactions which are void must be distinguished from speculative transactions which are generally valid in law. As Farran J. said in *Todd v. Lakhmidas* (j), "there is no law against speculation, as there is against gambling". This is because all business necessarily involves some sort of speculation. Even in case of ready goods (called "*ready transactions*"), a dealer who purchases them, wholesale or otherwise, against cash, does so in the legitimate hope that he would be able to dispose of the goods in future at a profit. In other words, he speculates on the rise or fall of the market. The same is true with regard to transactions for future goods (known as "*forward*" or "*Vaida*" transactions). A buys from B 100 bales of Broach Cotton for the Vaishakh vaida (settlement) at Rs. 100 per bale. This is a forward transaction under which A will be entitled to receive from B, 100 bales of the Broach Cotton on the settlement day for the Vaishakh vaida, on payment of Rs. 100 per bale only, though the actual market rate on that day may be Rs. 150 per bale. By this forward transaction, therefore, A has made a profit of Rs. 50 per bale. There is nothing wrong in doing this, as it is a legitimate business transaction, entered into by A for the protection of his own interest. Such forward transactions are entered into in all sorts of commodities, e.g. gold, silver, cotton, linseed, shares and stocks, etc. They are, in fact, the normal course of business in all commodities.

Cross Contracts: Such forward transactions of sale and purchase sometimes balance each other, when the settlement day arrives. Thus A having sold 500 bales of Broach Cotton for Rs. 100 per bale to B for the Vaishakh vaida, may have also bought an equal number of bales from B for the same vaida, though at different rates. In such a case these *cross contracts* of sales and purchases will balance each other, with the result that on the due date no delivery will have to be given or taken by A or B, but only differences in rates will have to be paid or recovered by A or B as the case may be. Such transactions are also legitimate transactions in law and not wagering transactions, there being a genuine intention to do honest business in their case. Sometimes a forward transaction is also *closed* by a *cross contract* before the due date has arrived. Thus A on 1st January having sold

100 bales of Broach Cotton to B for the Vaishakh vaida at Rs. 100 per bale finds on the 1st Maha the market going against him, with the rate at Rs. 125 per bale. He does not want to take further risk, in which case, on 1st Maha he can settle his outstanding contract of sale by a purchase of 100 bales of the same Vaishakh vaida at Rs. 125 and liquidate his loss at Rs. 25 per bale. This process may also be gone through on the settlement date also. Thus A having purchased from B 500 bales at Rs. 100 per bale for the Vaishakh vaida and the market rate being Rs. 150 on the due date, A and B may settle the transactions on the due date by "closing" the said transactions at the market rate of the day at Rs. 150, leaving only differences in the prices to be paid by one side to the other.

Dealing in differences: As shown above, the above transactions all result in the payment and receipt of the differences in the prices by one party to the other. They are highly speculative but they are not necessarily wagering transactions, *there being a genuine intention to do legitimate business behind them*. But there may not be such genuine intention in every case. The parties may only want to gamble on the rise or fall of the market. In such case the transaction would be a wagering transaction and therefore void. The test laid down by Bombay High Court in *Todd v. Lakhmidas (k)*, in order to decide whether a transaction is a wagering transaction or not is as follows: viz. "it must be the intention of both parties, at the time of entering into the contract, under no circumstances, to call for or give delivery from or to each other, but to settle the contract by payment of differences only". It is only if such intention is proved, that the transaction will be regarded as a wagering transaction or a "dealing in differences", otherwise not. The essentials of a wager, therefore, are (i) a common intention, i.e. of both parties, (ii) at the time of entering into the contract, (iii) under no circumstances, (iv) to call for or give delivery, but (v) to settle the transaction by payment of differences only. Each of these conditions must be fulfilled before a defence of wager can prevail. Thus if delivery is legally claimable under the contract, no wager can result. Further, intention to wager must exist at the time of entering into the contract and not afterwards. Lastly, where the intention to pay differences only, exists on the part of one party only and not on the part of both, there can be no wager. This is particularly so, where transactions are entered into through the medium of brokers, by parties who never meet each other at all.

Thus in *Perosha v. Manekji (l)*, Manekji purchased through plaintiff, a broker, government paper and shares of a certain mill worth lakhs of rupees for a particular "vaida". Plaintiff knew that the transactions were beyond the means of Manekji but as broker, the plaintiff himself had entered into genuine transactions with third persons on the defendant's instructions. Held, the defendant was bound by the transactions, because, however much it may be the defendant's intention to gamble on the market, he had failed to show that third parties with whom the plaintiff (as broker) had entered into the transactions on the defendant's behalf had also a similar intention. Similarly, in *Sassoon v. Tokersey (m)*, where large contracts in American Cotton for future delivery ("American futures") were entered into through Sassoons as brokers and it was found that the Sassoons had duly placed these contracts on the Liverpool Exchange with third parties on behalf of the defendants, it was held that there was no wager. On the other hand in *Doshi Talakshi v. Sha Ujamsi Velsi (n)*, a series of contracts for sale of Broach Cotton were entered into in Dhorela, where a new Cotton Exchange was established. It was proved on evidence that for a series of years, no contracts for such cotton were ever completed in the said market by giving or taking delivery but had been only settled by payment of differences only. In the case in question, no delivery had been

(k) 16 Bom. 441.
(l) 22 Bom. 899.

(m) 28 Bom. 616.
(n) 24 Bom. 277.

ever asked for or offered between the parties. *Held*, the transactions were wagering and therefore void. Similarly, in *Kong Yee Long and Co. v. Lowjee Nanji* (o), the defendant, a rice miller in Rangoon, with a factory capacity of 10,000 bags of rice a month, entered into a contract for supply of 2 lakhs bags of the aggregate value of 5 crores, to the plaintiff in 7 weeks. None of the transactions were performed by giving and taking delivery, but on the due date, defendant passed a promissory note in favour of the plaintiff for the difference in the prices. The capital of the defendant's company was Rs. 1 lakh and he had also entered into other contracts with third parties during the period. In a suit on the pro-note passed by the defendant as above, it was held by the Privy Council that the transaction was obviously a wager and the promissory note, therefore, could not be enforced by the plaintiff.

“Pakka Adatia” and Wager : The case may however be different where instead of an ordinary broker, e.g. a “Kachha Adatia”, a “Pakka Adatia” is employed to effect transactions. As Sir L. Jenkins pointed out in *Bhagwandas v. Burjorji* (p), a Pakka Adatia, though upto a certain stage, an agent, is by custom and usage of the market, in the position of a principal also. He is, therefore, entitled in law, to appropriate his own contract to the principals' business, without obtaining his previous consent thereto. A wagering agreement in the above sense, therefore, is possible in such a case, because both parties (the customer and the “Pakka Adatia”) are in the position of principals. Whether it is so in a given case, is, of course, a question of fact.

In the above case, Burjorji having won a lottery, began to speculate heavily on the linseed market. In June-July, he sold through plaintiff, a Pakka Adatia, 4,000 tons of linseed for September delivery, which instructions were duly carried out by the plaintiff by means of 79 contracts. Rs. 61,000 were deposited by the defendant with the plaintiff as margin money. In August the market went against the defendant. The plaintiff asked the defendant for delivery of linseed or to authorise the plaintiff to purchase linseed on the defendant's behalf. The defendant, however, did neither. The plaintiff, therefore, himself delivered 300 tons and balanced the rest by cross contracts. In a suit to recover the loss paid by the plaintiff on behalf of the defendant, *held*, by the Privy Council, that the fact that the defendant was known to the plaintiff as a speculator was not enough and that in the absence of express or implied agreement between the two, under no circumstances to call for or take delivery under the contract, the transactions could not be regarded as wagering transactions.

“Teji Mandi” Transactions : The Courts at one time looked upon these transactions with very great disapproval, so much so, that the appearance of any one of the above terms in any contract was sufficient to condemn it as wagering contract. Latterly, however, the attitude has changed and the rule now followed is that a “Teji” or a “Mandi” or “Teji Mandi” transaction is not necessarily a wagering transaction but that if a common intention to wager is proved with regard thereto, it will be regarded as such. Two causes have provoked this change : (i) the true nature of such transactions is now more fully understood, and (ii) it has been found, on evidence, that in case of such transactions, deliveries are often given and taken. The *modus operandi* of these transactions is as follows : A buys 100 bales of cotton from B for a particular vaida at Rs. 100 per bale. A is apprehensive that on the due date, the market may go against him, i.e. may go down to Rs. 90 per bale. He therefore applies, or as it is called, “purchases” “Teji” at Re. 1 per bale. What A does thereby is to ‘purchase an option’ (in return of the payment of Re. 1 as above) not to buy the 100 bales on the due date, i.e. an option to cancel the contract of purchase with B (which, otherwise, he is bound in law to carry out), if the market, in fact, turns out to be against him on the due

date. If, for instance, the market rate on the due date is Rs. 90 per bale, A will exercise his option to cancel the contract, so that his possible loss of Rs. 10 per bale disappears, leaving him liable to pay the "Teji" only, i.e. Re. 1 per bale. If the market on the due date is in A's favour, i.e. Rs. 110 per bale, A will not exercise the option, and thus pocket the profits of Rs. 10 per bale, paying only Re. 1 per bale as "Teji". In applying "Mandi" the process is reversed. In this case the person purchasing "Mandi" secures an option to cancel the contract, if the market is against him on the due date, e.g. if being a seller, the market goes up. He thus protects himself against a possible rise in the market, as the purchaser of a "Teji", in the first case, protects himself against a possible fall in the market. In "Teji Mandi", a *double option* is purchased. The person can be either seller or buyer, at his choice, on the due date, according to the exigencies of the market. Thus understood, "Teji" and "Mandi" and "Teji Mandi" transactions are really insurances against the fluctuations of the market, which traders, having legitimate business to protect, are not debarred by law from entering into (q). If, however, in such cases, it is proved that the parties had agreed never to call for or take delivery at all under the contracts, the transactions would be wagering transactions and therefore, void under the sec. (r). "Teji Mandi" transactions may be compared with the "put and call" transactions, which are frequently effected on European Exchanges.

By the Securities Contracts (Regulation) Act 42 of 1956, "dealings in options" in securities like shares, stocks and Co. debentures and in Government securities, and Teji Mandi contracts in respect of the same are made illegal.

PROOF OF WAGER: It will be seen that when the question of wager is raised, the Court has to determine what the real intention of the parties was. The following rules have been laid down in this connection: (i) the intention need not be expressed, as in most cases it never is, the question being dependent on inferences from known facts (s). (ii) The Court is not bound by the written terms of a contract, but is entitled to go behind it, to find out the true intention of parties (t). (iii) The Court will look at all the surrounding circumstances, in particular (a) the position and means of the parties (u); (b) general nature of the party's business (v); (c) conduct of the parties themselves (w); and (d) evidence of other contracts of similar nature in the same market to show whether delivery is usually taken and given or not (x).

Wager and collateral transactions: Though a wagering contract is void and no suit can lie to recover the fruits of a wager, transactions incidental to a wagering transaction are not made void by the sec. Thus a broker in a wagering transaction can recover his brokerage (y). Similarly, if he has paid losses on behalf of his principal in respect of wagering transactions, his claim for indemnity therefor against the principal is maintainable (z). Moneys lent and advanced for the purpose of wagering transactions are also recoverable in spite of sec. 30, so also moneys paid to pay off a gaming debt (a). Can a cheque given to pay off a wagering loss be enforced? It has been held that it cannot be, since the wagering contract being void, there is no consideration for the cheque. It has been held in Calcutta, however, that

(q) Manubhai v. Keshavji, 24 Bom. L.R. 60.

(r) Sobhagchand v. Mukunchand Balia, 53 I.A. 241.

(s) Kong Yee Long & Co.'s Case (Supra).

(t) Re Gieve (1899), 1 Q.B. 794.

(u) Kong Yee Long's Case (Supra).

(v) Moulal v. Govindram, 7 Bom. L.R. 385.

(w) Ibid.

(x) Sassoon v. Tokersey (Supra).

(y) Jagat Narain v. Shri Krishna, 33 All. 219.

(z) Daya Ram v. Murli Dhar, 49 All. 926.

(a) Subba v. Devendra, 7 Mad. 301.

a principal can file a suit against his agent to recover prize money received by him on account of a wagering transaction (b).

Bombay Act III of 1865: In Bombay Presidency, however, a different rule prevails by reason of Act 3 of 1865. Under this Act "all contracts to further or assist, entering into contracts by wager or gaming, and all contracts by way of security or guarantee for the performance of such agreement are null and void". Secondly, under the Act, no suit can be brought to recover commission or brokerage or reward in respect of such transactions. Thus a deposit paid in respect of wagering contract cannot be recovered in Bombay (c). In Bombay Presidency even transactions collateral to wagering transactions are void. This is not so elsewhere. In this respect, Bombay Law follows English Law. It has thus been held in England that when an agreement to pay a betting debt is void, an action based on an account stated in respect of those bets cannot be maintained. An agent therefore of the bettor cannot recover from the principal amounts paid by him on the latter's behalf to the bookmaker, as on an account stated between him and his principal (d). Even if there is an entirely new consideration for the payment of a gaming debt, yet, if what is agreed to be paid is in fact a gaming debt, the plaintiff cannot recover under the contract (e). Similarly, where a charge was created for a gaming debt which contained also a personal covenant to pay, it was held that the charge holder could not, on the charge being held void under the Gaming Act, rely only on the covenant to make the defendant liable (f). Money lent to another with knowledge that it was to be applied by the borrower in paying gambling losses also cannot be recovered (g). Even in Bombay Presidency, however, the original transaction must be proved to be a wagering transaction, before the principle of the Act can apply (h).

Wagering transaction when good: Under cl. (2) to sec. 30, an agreement to subscribe or contribute for or towards a plate, prize or sum of money, of the value of Rs. 500 or upwards to be awarded to the winner of a horse race is valid. This, however, does not make betting on such a race or horse valid. Similarly, a lottery, even if authorised or sanctioned by Government, does not give rise to a valid contract (i).

Contingent Contract (sec. 31)

This is defined by sec. 31 as "a contract to do or not to do something, if some event, collateral to such contract, does or does not happen". Quite a good part of commercial business transactions consists of contingent contracts; hence the necessity for a separate treatment for such contracts. They are also known as "conditional contracts". In such contracts, the liability is not absolute but dependent upon the happening or not happening of a certain event, e.g. arrival of a ship, production by a particular mill, etc. Ordinary contracts of insurance are also contingent contracts, so also contracts of guarantee and indemnity. It is important to note in this connection that it is not every contract in which liability is dependent on a contingency that can be called a contingent contract. Thus A's promise to pay Rs. 500

(b) *Kshitendra v. Madaneshwar*, 63 Cal. 1234.

(c) *Dayabhai v. Lakmichand*, 9 Bom. 358.

(d) *Law v. Dearnley* (1950) 1 All. L.R. 124.

(e) *Hill v. William Hill* (1949) 2 All E.R.

452.

(f) *William Hill Ltd. v. Hoffman* (1950)

1 All E.R. 1013.

(g) *Macdonald v. Green* (1950) 2 All E.R. 1240.

(h) *Chimanlal v. Niyamatrai*, 39 Bom. L.R. 1083.

(i) *Dorab Tata v. Lance*, 19 Bom. L.R. 697.

to B if B marries C, is not a contingent contract at all but merely an offer, which becomes a concluded agreement when B marries C. In other words, if the contingency is of the essence or foundation of the contract, there is no case for a contingent contract. It is only if the contingency is as regards a matter 'collateral', i.e. incidental to the main purpose of the agreement, that the contract can be called a "contingent contract". Thus a builder's contract with a stipulation that payments shall be against the architects' completion certificate, an insurance company's contract to pay "if claim is properly made and proved to the directors' satisfaction" are contingent contracts. Notice in this connection that a contingency dependent on the mere will and pleasure of one of the parties to the contract is not enough. Thus an agreement to work on such payment as the employer pleases to make, is no contract at all. The contingency must be dependent on the act of a party, even though the act is voluntary or discretionary. Thus an agreement to pay "as A shall decide", is a good contract. A under the agreement is bound to exercise his discretion honestly and not capriciously.

Rules as regards contingent contracts (secs. 32-36): The above secs. lay down certain elementary rules as regards performance of contingent contracts which are as follows: (1) If the contingency is the happening of an uncertain future event, the contract cannot be enforced till that event happens. If the event becomes impossible, the contract becomes void (sec. 32). (2) If the contingency is the not happening of an uncertain future event, the contract can be enforced only when the happening of that event becomes impossible (sec. 33). (3) If the contingency depends on the way a person will act at an unspecified time, the event will be considered to become impossible, when the person acts in such a manner that it becomes impossible for him to act as specified, within a definite time or otherwise than under further contingencies (sec. 34). Thus A promises to pay B Rs. 500, if B marries C. B's marriage with C becomes impossible, if B marries D, because, though D may die, and B may marry C, no definite time can be fixed as regards the happening of the event, which again is contingent, i.e. problematical. (4) If the contingency depends on a specified uncertain event happening within a fixed time, the contract becomes void, if such thing does not happen or becomes impossible before the fixed time. (5) If the contingency depends on a specified uncertain event not happening within a fixed time, the contract can be enforced if such event does not happen or becomes impossible of happening before the fixed time (sec. 35). (6) An agreement to do or not to do anything, if an impossible event happens, is void, whether the impossibility was known or unknown to the parties at the time of the contract (sec. 36), e.g. an agreement to discover treasure by magic.

CHAPTER IV

PERFORMANCE OF CONTRACTS

Discharge of contracts: Having considered (in secs. 10-36) how a contract can be entered into, the Act in the secs. following, i.e. secs. 37-67, deals with the question, viz. how a contract can be discharged. A contract can be discharged in a variety of ways: (i) by performance; (ii) by a new agreement in place of the old one; (iii) by impossibility of performance; and (iv) by acceptance of breach. Secs. 37-58 deal with the question of performance of contract.

Obligation to perform a contract (secs. 37-38): Sec. 37 lays down an elementary rule, which, however, has important consequences in law. The sec. provides that the parties to a contract must either (i) perform their respective promises or (ii) offer to perform the same, unless (iii) such performance is dispensed with or (iv) excused under the provisions of any law. In other words, every valid contract must be duly carried out by parties thereto, each party carrying out its respective part of it. If a contract is not carried out, the least that each party is bound by law to do, is to offer to perform his part of the contract to the other. Exception is made in two cases only, viz. where performance is dispensed with or where it is excused by law. The latter case is considered by sec. 39, the former by secs. 62-67. What an "offer to perform" must contain is dealt with by sec. 38.

Liability of representatives [sec. 37, cl. (2)]

The sec. further provides that the liability of performance devolves, on the death of the promisor, on his representatives, unless a contrary intention appears from the contract. Generally, contracts bind the executors and administrators of the deceased promisor though, of course, their liability is limited to the estate of the deceased which has come to their hands. An exception is made where personal considerations have entered in the making of the contract, e.g. a contract of agency or of service or where the contract involves personal skill on the part of one of the parties thereto, e.g. a contract to paint a picture. These contracts, by their very nature, do not devolve on the heirs and legal representatives of a deceased promisor, because performance by such substituted parties will not accord with the intention of the original parties to the contract.

Succession to the benefit of contract

The Act nowhere deals with this question as regards a succession to the benefit of a contract. Generally, the benefit of a contract devolves on the legal representatives of a promisee, in case of his death before performance and such representatives, therefore, are entitled to enforce the performance of the contract against the promisor. Exceptions are in case of contract involving personal skill or other considerations of a personal nature, e.g. a contract to marry. Sec. 306 of the Succession Act may be mentioned here, according to which, all causes of action existing for or against a person at the time of his death, survive to or against his legal representatives, except causes of action for (i) defamation, (ii) assault, or (iii) other personal injuries not causing death, and (iv) cases where granting relief after death would be nugatory, e.g. breach of promise of marriage.

Assignment of contracts

On this subject also, the Act provides no specific rules. A contract may be assigned (i) by act of parties or (ii) by operation of law. As regards (i), a general rule, established by decisions, is that the benefit of a contract can be assigned but not its burden (j). Thus a debt can be assigned by a creditor to a third person without the consent of the debtor. Provision for this is made by sec. 130 of the "Transfer of Property Act" which deals with transfer of actionable claims. An "actionable claim" is defined as a "claim to any debt, other than a debt secured by a mortgage of immoveable property, or by hypothecation or pledge of moveable property

(j) *Tolhurst v. Associated Cement Manufacturers* (1902), 2 K.B. 660.

or to any beneficial interest in moveable property not in the possession of the claimant" (sec. 3, Transfer of Property Act). A debt is an "actionable claim". The assignment of a debt by the creditor must be in writing, signed by the transferor or his duly authorised agent and the transferee must give express notice of the transfer to the debtor before such transfer is effective against him. The transfer is also subject to all equities existing at the date of the transfer as against the transferor. A debtor, however, cannot assign his liability to a third party, without the consent of the creditor. This would require "novation" as defined by sec. 62 of the Contract Act. Even in the case of a benefit under a contract, the rule, as regards its assignability, is not without exceptions. Thus where personal considerations have entered into the making of a contract, the promisee cannot assign his benefit under the contract to another person. Where in a contract for the purchase and sale of salt, the terms were that the vendor was to supply, for 7 years, salt in such quantities as the purchaser required, certain credit being given to the purchaser, and the purchaser also undertook to make petty repairs, it was held that the purchaser could not assign the benefit of the contract to another (k).

Can a contract for future performance be assigned? The question has arisen in connection with forward contracts for sale or purchase of goods. It has been held that the buyer's interest under a forward contract can generally be assigned by him, as being an "actionable claim" under sec. 130 of the Transfer of Property Act (l). It would be otherwise, however, if the benefit is coupled with a liability or if personal considerations have entered into the making of the contract (m). Can the seller's right to compel the buyer to pay the price be assigned? The point is not decided. It has been held, however, that the seller's right to claim damages against the buyer for breach is not assignable as this is not an "actionable claim" and being a "mere right to sue" cannot be transferred under sec. 6 of the Transfer of Property Act (n). There are special provisions for assigning certain classes of contracts, e.g. Negotiable Instruments, shares in a company, a bill of lading, under the Bill of Lading Act, and Life and Marine Insurance Policies, which can be assigned under special provisions relating thereto in the Transfer of Property Act (see seq.) (ii) Contracts can also be assigned by operation of law: e.g. (a) on death and (b) on insolvency. The death of a party passes all his rights of action to the legal representatives, except in certain cases (see ante). In case of insolvency, all rights and liabilities of the insolvent pass to the Official Assignee or Receiver, as the case may be.

Essentials of a valid offer of performance (sec. 38)

Sec. 38 provides that if an offer of performance is duly made by a party and it is not accepted by the other side, the promisor (i) is not liable for non-performance of the contract and (ii) he does not lose his rights under the contract (i.e. the right to claim specific performance and/or damages against the other party). Such an "offer of performance", however, must fulfil the following conditions: (i) it must be unconditional; (ii) it must be made at the proper time and place and under circumstances which would show the other party that the offeror was able and willing, there and then, to fulfil the whole of his promise; (iii) if the offer is to give delivery, reasonable opportunity must be given to the offeree to see that the thing offered

(k) *Namasivaya v. Kadir*, 17 Mad. 168.

(l) *Hansraj v. Nathu*, 9 Bom. L.R. 838.

(m) *Jaffer v. Budge Budge Jute Mills*, 33

Cal. 732.

(n) *Abu Mahomad v. Chunder*, 36 Cal. 345.

is the thing which the offeror promised to deliver ; (iv) an offer to perform to one of several joint promisees, is a valid offer of performance. To this may be added (v) it must be an offer to perform the whole and not a part of the promise.

“Tender”

An “offer of performance” is sometimes called “tender”. In order that a “tender” may be valid, it must fulfil all the above conditions. It must be of the whole and not of a part of the amount due. Thus an offer to pay Rs. 90 with a promise to pay Rs. 10 hereafter, when Rs. 100 are due, is not a valid tender. The creditor is entitled to reject such part payment. No conditions should be attached to a tender. A tender of money in full satisfaction of the amount due, however, is not invalid, as the creditor is not thereby required to accept any condition (o). The exact amount due should be tendered. A tender of a larger amount, with a demand for change, is not a valid tender. Thus in Calcutta, a tender of a Rupee note in payment of 1 anna fare, with a demand for change, has been held to be invalid (p). A tender may be made under protest, so as to reserve the right of the payee to dispute the amount.

“Able and willing”: cl. (2): These words have a peculiar significance. Actual production of the amount is necessary. An offer to give a cheque is not a proper offer to perform, unless the creditor has agreed to accept payment by cheque. As regards furnishing a reasonable opportunity for examining the goods, what is “reasonable opportunity” is a question of fact. In a Bombay case, a day’s time was held quite sufficient, where a sale of cotton bales was concerned (q). A tender to one of several joint promisees is good as “tender” but is not sufficient to secure a complete discharge of the contract (see sec. 45) (r). The object of tender is to show that the party making the tender was ready and willing to perform his part of the contract and was only prevented from doing so by the act of the other party. Thus if the goods are tendered and refused by the buyer, the seller is discharged from all liability. In case of money, however, the tender must be followed by payment of the amount into Court, on an action being brought against the party for breach. It has been held by the Privy Council that in order to show readiness and willingness it is not necessary for the buyer to actually produce the moneys or vouch a concluded scheme for financing the transaction (s).

Refusal to perform (sec. 39)

The above sec. deals with the question as to when a promisee may put an end to the contract. Under the sec., when a party to the contract has (i) refused to perform or (ii) disabled himself from performing the contract (iii) in its entirety, the promisee may put an end to the contract, (iv) unless he has signified, by words or conduct, his acquiescence in its continuance. Two conditions are essential, therefore, before a promisee can exercise his right under the sec.: (i) the other party must have either refused or disabled himself from performing the promise and (ii) the failure must be of performing the promise “*in its entirety*” or wholly or completely and not as to a part of it only. If these two conditions are satisfied, the promisee is

(o) Bowen v. Owen (1847), 11 Q.B. 130.

(p) Bireswar v. King Emperor, 46 C.W.N. 550.

(q) Ratansi v. Jamnadas, 6 Bom. 692.

(r) Sitaram v. Shridhar, 27 Bom. 292.

(s) Bank of India Ltd. v. Chinoy, 77 I.A. 76.

given two rights or, more correctly, an option, e.g. (i) either to treat the whole contract as broken, to put an end to it on that ground and to claim damages against the other party as on a breach of the whole contract, or (ii) to treat the contract as alive, accept performance of it (if made) by the other side and claim damages (if any) for only such part of the contract as has not been performed. This is called "*waiving the breach*" or "*acquiescing in the continuance of the contract*", after its breach by the other side. Thus, as the illustrations show, in a seasonal contract for two months, with two appearances each week, if the artist wilfully absents herself on the sixth night, the theatre manager is entitled, if he so chooses, to cancel the whole of the remaining contract and claim damages on that basis. If, however, he allows the artist to sing on the seventh night, he has, in effect, "*waived the breach*" or has acquiesced in the continuance of the contract, and therefore, he will not thereafter be entitled to cancel the contract on the above ground. His right to claim damages for wilful failure of the artist to appear for one night is, of course, not affected.

The right given by the sec. can be availed of by a promisee when (i) the promisor refuses to perform or has disabled himself from performing his promise (ii) in its entirety. Thus if on a contract of sale of goods, the purchaser informs the seller, without just cause, that he will not take delivery, it amounts to a wrongful repudiation of the contract by the purchaser. The seller, under the circumstances, is absolved from the liability of tendering the goods and further, he can sue the buyer for damages for breach of the whole contract. Similarly, if A after an agreement to sell his house to B, sells the house to C, thus "*disabling himself*" from selling the house to B, B can put an end to the contract and sue A for the whole breach (t). Notice, however, that the refusal or disability to perform must be of the contract "*in its entirety*", i.e. of an integral part of the contract (u) and not of a subsidiary part thereof (v).

Thus where a contract was entered into for sale of sugar to be delivered in two instalments, and the first shipment having arrived and being tendered, the purchaser refused to accept and pay for the same, it was held that this did not justify the seller in refusing to tender the second shipment on arrival, when the purchaser was ready and willing to accept and pay for the same (w). On the other hand, where on a sale of straw to be delivered by instalments, payment to be against each load of straw as delivered, the purchaser subsequently failed to pay for certain deliveries, and on being pressed by the seller to do so, paid all the arrears except the price of one load, claiming to hold the same as security for the due performance of the contract, the Court held that this amounted to a total refusal by the purchaser to perform the original contract between the parties and the seller was, therefore, justified in putting an end to the contract and refusing to deliver any more straw to the plaintiff under the same and claiming damages against him as on a breach of the whole contract (x).

With regard to *instalment contracts*, notice that though ordinarily refusal to pay for or give delivery of one instalment, will not justify the other party in putting an end to the contract, the refusal may be accompanied by such circumstances, or may be so frequent, as to show a clear intention of not performing the contract at all. In such a case the other party is entitled to put an end to the whole contract (y) (see sec. 38, Sale of Goods Act). Secondly, a "*refusal to perform*" which is conditional, the condition being

(t) *Synge v. Synge* (1894), 1 Q.B. 466.

(u) *Withers v. Reynolds* (1891), 2 B. & Ad. 882.

(v) *Freeth v. Burr*. (1879), L.R. 9 C.P. 208.

(w) *Rashbihari v. Nritya Gopal*, 33 Cal. 477.

(x) *Withers v. Reynolds* (Supra).

(y) *Homeswar Sing v. Juggal Kishore*, 28 Bom. L.R. 187.

to the Calcutta, Madras and Bombay High Courts no second suit lies in such a case (g). The reason is that there being only one cause of action in case of a joint promise, the same becomes merged in the decree when passed. The Allahabad High Court has held otherwise (h), as according to it, sec. 43 creates separate causes of action against joint promisors in respect of the same debt. The former, however, appears to be the better view. Of course, a judgment by consent against a joint promisor is no bar against the other joint promisors in the same suit, even in Bombay (i). Notice further that co-heirs are not joint promisors. They must be all joined in the suit (j).

Contribution between joint promisors: The right of contribution given by cl. (2) of sec. 43 to joint promisors has been held in England to be subject to the qualification that there can be no contribution as between joint tortfeasors, i.e. between persons who jointly commit a civil wrong. This is called the rule in *Merryweather v. Nixon* (1799), 8 T.R. 186. The rule has been adversely criticised in England and has been held to be not applicable at all to India (k).

Joint promisees (sec. 45)

Sec. 45 provides for devolution of joint rights, in case of joint promisees. According to the sec., where a person has made a promise to two or more persons jointly, then, unless a contrary intention appears from the contract, the right to claim performance rests, as between them, with them jointly, during their joint lives and after the death of any one or more of them, with the representatives of the deceased and the survivors jointly and on the death of the last survivor, with the representatives of all jointly. In other words, in case of a promise to two or more persons jointly, such persons jointly and on the death of any one or all of them, the survivors and the representatives of deceased jointly, are the only persons who are entitled to claim performance of the promise. The sec. applies to partners, co-sharers, co-mortgagees and, in fact, to all cases of joint creditors. They must all join together to claim performance of the promise. If some only join, their suit is liable to be dismissed under the provisions of the sec. It may happen, however, that all the co-promisees are either not able or not willing, to join in making the claim. Where such is the case, the proper procedure to be adopted is to make such persons, party defendants to the suit. Where this is done, the Court will have before it all the parties necessary to give a valid discharge to the debtor and the objection as regards non-joinder will disappear.

To the above rule as regards devolution of joint rights, there are a few exceptions: (i) it has been held that in case of a debt due to a partnership, the surviving partners alone can sue to recover the same, without joining the heirs of the deceased partner with them (l). This has been now also provided by O. 30, r. 4 of the Civil Procedure Code. (ii) In case of Government securities, under the Government Securities Act (X of 1920), where a Government security is payable to two or more persons jointly, the same shall be payable to the survivor or survivors of them. Notice that it is clear under the terms of the sec., that a payment of a debt by the debtor to one

(g) *Hemendra v. Rajendralal*, 3 Cal. 353; *Gurusami v. Samutti*, 5 Mad. 37; *Shivlal v. Birdichand*, 19 Bom. L.R. 370.

(h) *Muhamad v. Radheram Sing*, 22 All.

307. (i) *Markandrai v. Virendrarai*, 19 Bom.

L.R. 837.

(j) *Shaikh Sahad v. Krishna Mohan*, 24 Cal. L.J. 371.

(k) *Venkata v. Venkaya* (1942), 2 M.L.J.

427.

(l) *Motilal v. Ghelabhai*, 17 Bom. 6.

of the joint creditors will not operate as a good discharge for the debtor. It has been so held by the Calcutta (m) and the Bombay High Courts (n). The Madras High Court, however, has held otherwise (o).

Time and place of performance (secs. 46-50)

The above secs. lay down elementary rules as regards the time when and the place where a contract is to be performed. The rules are: (i) where no time for performance is fixed by the contract and the promisor is to perform the promise without application by the promisee, the promisor must perform the promise within a reasonable time. What is reasonable time must depend upon the facts of each case (sec. 46). (ii) Where the date of performance is fixed and the promisor is to perform the promise without application by the promisee, the promisor must perform the promise on that date, during the usual business hours and at the place where it ought to be performed (sec. 47). (iii) If date of performance is fixed but the promisee is, under the contract, bound to apply for performance, the latter must demand performance on that day, at the proper place and within the usual business hours (sec. 48). (iv) Where no place of performance is fixed and the promisor is bound to perform without application by the promisee, the promisor is bound to apply to the promisee to fix a reasonable place for performance and to perform at that place (sec. 49). This sec. may be compared with the previous sec., whose obverse it is intended to be, though it hardly succeeds in its object. The sec. is important from the point of view of jurisdiction. The general rule of Common Law with regard to payment of a debt is that, where no place of payment is mentioned, the debtor is bound to find the creditor and pay him at his place, if within the realm (p). Where no place for performance has been fixed therefore, and there is no provision to perform without application, the place where the cause of action can be said to have arisen would be the place where the creditor resides (q).

The validity of the application of the above Common Law rule, however, has been doubted by the Privy Council, in *Soniram v. R. D. Tata & Co.* (r). In their Lordships' opinion, the rule has been superseded by the express provisions of sec. 49. It has been recently held by the Court of Appeal in Bombay that the sec. does not apply to negotiable instruments, e.g. a promissory note, which is governed by the Negotiable Instruments Act (s). The sec. does not get rid of inferences which may justly be drawn from the terms of the contract itself or from the necessities of a case involving in the obligation to pay the creditor, the further obligation of finding the creditor, so as to pay him. Thus where a contract was made in Calcutta, under which the defendants agreed to make good to the plaintiffs all loss caused to the latter by the default of the defendants' customers in Rangoon, where the plaintiffs had their office, it was held, by the Privy Council, that the Rangoon High Court had jurisdiction to try the case, as that was impliedly the place where the loss was to be made good (t).

Lastly, performance of a promise may be made in any manner or at any time which the promisee prescribes or mentions. Thus though a payment by cheque is always a conditional payment, if the cheque is agreed to be accepted by the promisee as due performance of the promise, payment by cheque would operate as a complete discharge. Similarly, if the promisor

(m) *Jagat Tarini v. Naba Gopal*, 34 Cal. 305.

(n) *Sitaram v. Shridhar*, 27 Bom. 292.

(o) *Barbar v. Ramana*, 20 Mad. 461.

(p) *Haldane v. Johnson*, 8 Ex. 689; *Bansilal v. Ghulam Mahboob*, 53 I.A. 58.

(q) *Motilal v. Surajmal*, 6 Bom. L.R. 1038.

(r) 20 Bom. L.R. 1027.

(s) *Jivatlal v. Lallbhai*, 44 Bom. L.R. 495.

(t) *Soniram v. R. D. Tata & Co.*, 54 I.A. 265.

requires payment by post, posting a letter containing the money, duly addressed to the promisee, will be effective discharge of the promise [sec. 49, ill. (a)].

Performance of Reciprocal Promises (secs. 51-58)

These secs. deal with certain rules governing the performance of reciprocal promises. As pointed out before, a majority of commercial transactions consist of such promises; hence the importance of these rules. Reciprocal promises may be of three kinds: (i) promises to be simultaneously performed. These are dealt with in sec. 51; (ii) conditional or dependent promises or promises in which the performance of one depends upon the performance of the other. These are dealt with by secs. 52-54. (iii) Mutual but independent promises. There is no provision in the Act relating to such promises.

Promises to be simultaneously performed (sec. 51): Under sec. 51, where a contract consists of reciprocal promises to be simultaneously performed, the promisor need not perform his promise, unless the promisee is ready and willing to perform his reciprocal promise. Thus if goods are sold, cash against delivery, the seller need not deliver, if the buyer is unable to pay cash. Similarly, the buyer need not pay cash, unless the seller is ready and willing to deliver. A contract for sale of shares to be transferred to the name of the purchaser on payment of price on a fixed date also requires concurrent performance. Whether in a given case, promises are such as would require simultaneous performance, is a question of fact. The question here considered is different from one arising under sec. 39, under which a failure on the part of one party to perform his part of the contract, entitles the other to "put an end" to it, i.e. rescind it. Notice that "ready and willing" as used by the sec. does not require that the promisor concerned should have the actual physical possession of the subject-matter of the contract. It is enough if he has control over it or the means of control over it, sufficient to enable him to give delivery thereof to the other party or cause delivery so to be given to that party. Thus on a contract for the sale of shares, it is sufficient evidence of "readiness and willingness" on the part of the seller, if he tendered to the buyer, the allotment letter together with blank transfers signed by the original allottee with an application signed by the latter requesting a transfer (u). To prove "readiness and willingness", it is not necessary to prove actual tender also (v). Indeed, if the purchaser, before the due date, has refused to take delivery and thus repudiated the contract, no tender at all may be necessary (w).

Conditional promises (secs. 52-54)

In case of such promises, sec. 52 lays down that if the contract fixes an order of performance, they should be performed in that order; if no order is fixed they should be performed in their natural order.

Thus under a contract to build, the builder must first build, before he can claim payment for the services rendered by him. On the other hand, where A promises to hand over the stock-in-trade of his business to B for a price and B promises to give security for payment of the price, the security must be given first by B, before A can be called upon to hand over the stock-in-trade to him.

(u) *Imperial Banking Co. v. Atmaram*, 2 Bom. H.C.R. 246.

(v) *Imperial Banking Co. v. Pranjivandas*,

2 Bom. H.C.R. 258.

(w) *Shriram v. Madangopal*, 30 Cal. 865.

Two other rules are laid down with regard to such promises by secs. 53 and 54 : (i) Under sec. 53, where a contract consists of reciprocal promises, and one party thereto prevents the other from performing his promise, the contract becomes voidable at the instance of the party so prevented and such party can sue the other party in damages as well. Thus where on a sale of an excavating machine, the vendor agreed to give a trial performance to the satisfaction of the purchaser but the purchaser failed to provide conditions for a fair trial, it was held that it was the purchaser who was in the breach and that the vendor was entitled to damages against him (x). Similarly, on a sale of timber, the seller agreeing to fell and bundle the same, if the vendor fails to do either, the purchaser would be entitled in law to avoid the contract (y). (ii) The next rule is laid down by sec. 54, which provides that where in case of reciprocal promises, the nature of the promises is such that one of them cannot be performed or its performance cannot be claimed till the other is performed and the promisor of the last mentioned promise fails to perform his promise, such promisor cannot claim performance from the other party and must make compensation to him, for his own non-performance of the contract. Thus under a contract of charter party, if the charterer fails to produce the cargo, he cannot claim performance of the contract from the shipping company, and must pay damages to them for his failure to perform his part of the contract. The question in each case is whether the failure goes to the root of the contract. If it amounts only to a partial failure of the consideration for the contract, the sec. will not apply and the claim would only be for damages for failure to perform a part of the agreement (z).

Whether a contract is conditional depends on the construction of its terms. Thus where there was a contract for sale of parachute cloth, "January-February shipment", "the goods to be given delivery of when they arrived." *held*, the last words referred to the performance of the contract and did not make the contract conditional at its inception (z1). Where reduction of the terms of a contract to writing is one of the terms of a contract, such a term may be a "condition" of the contract; so that, if the terms of the contract are not reduced to writing by reason of disagreement, it can be said that there was no contract in fact (z2).

Time Essence Contracts (sec. 55)

These are contracts in which the time fixed for performance is regarded by the parties as of the essence of the contract, so that if the performance is not made at the stipulated time, the other party can treat the whole contract as broken and claim damages on that footing. In England, numerous rules are laid down by decisions as to when and under what circumstances the stipulation as to time of performance of a contract shall be regarded as an essential term of the contract. The present sec. cuts boldly across these rules and lays down one general and comprehensive rule for all cases, viz. that where a party to a contract promises to do a certain thing at a specified time or times, and fails to do so, the contract becomes voidable at the instance of the other party "if the intention of the parties was that time should be of the essence of the contract". "If such was not the intention,

(x) *Macay v. Dick*, 6 App. C. 251.

(y) *Giles v. Edwards*, 7 T.R. 181.

(z) *Oxford v. Proband*, 1 L.R. 2 C.P. 135.

(z1) *Ranchoddas v. Nathumal*, 51 Bom. L.R. 256.

(z2) *Thaverdas v. Union of India* (1955), 2 Mad. L.J. (S.C.) 23.

the contract is not voidable because of failure to perform at the agreed time, but the other party would be entitled to damages for loss caused by such failure to perform at the stipulated time". A further rule laid down by cl.

(3) of the sec. is this: if the contract being voidable on account of the promisor's failure to perform it at the agreed time, the promisee accepts performance thereof after the stipulated time, he will not be entitled to claim compensation for the promisor's failure to perform it at the time agreed, unless he has given notice of such intention on his part to the promisor at the time of accepting performance from him. In thus making the whole question depend upon the intention of the parties, the sec. does not lay down any new rule. English distinctions with regard to time essence contracts are also based on the same principle. Thus in England it has been held that in contracts for the sale of immoveable property, the presumption is that time was not intended to be of the essence of the contract unless (i) there is a stipulation to the contrary; (ii) the nature of the property is peculiar or unless (iii) surrounding circumstances constrain the Court to hold otherwise in equity. On the other hand, in contracts for the sale of goods, time will generally be regarded as of the essence of the contract, unless the parties otherwise agree or unless their conduct shows a contrary intention. In other mercantile contracts, there is no presumption either way, and each case will have to be decided on its own facts. These distinctions have also been followed in India (a).

Notice that even where time is not of the essence of a contract, there is nothing to prevent parties subsequently from making it so, e.g. by reasonable notice to the other side. On the other hand, if both parties delay inordinately in giving and demanding performance, that may be clear evidence of an abandonment of the contract (b). Agreeing to perform "as soon as possible" has been held to mean "within a reasonable time" in accordance with the usual course of business (c).

Notice that where a breach of contract has occurred under the sec., the date of breach cannot be extended, because after the breach, the promisee has kept the contract open. Thus if delivery is to be made on the 1st of January and it is not so made, the date of breach is 1st January. The fact that thereafter the buyer made repeated demands on the seller to supply the goods and the seller repeatedly promised to supply them to the buyer (but ultimately failed to do so), will not extend the date of breach to the later date, unless a clear agreement between the parties to extend the time of performance to such a date is proved. This was laid down by the Bombay High Court in the recent case of *Anandram v. Bholaram* (d). Where, however, such an agreement to extend time does finally come into existence between the parties, it does not matter that there were gaps in the intervening period, when there was only a one-sided extension of time (e). Where there is an agreement to extend time of performance, and that is broken, damages are to be calculated as of the extended date. For recovering of such damages, no notice as required by cl. 3 of the sec. is necessary. The notice therein referred to, refers to damages for breach of the original agreement (f).

(a) *Jamsed v. Burjorji*, 43 I.A. 26.

(b) *Pearl Mills v. Ivy Tannery Co.* (1919), 1 K.B. 78.

(c) *Hydraulic Engineering Co. v. Mc Haffie*, 4 Q.B.D. 670.

(d) 47 Bom. L.R. 719.

(e) *Paper Sales Co. v. Chokhani Brothers*, 48 Bom. L.R. 274.

(f) *Mahomad Habibulla v. Bird & Co.*, 48 I.A. 175.

Impossibility of performance (sec. 56)

Two cases of impossibility are provided for by sec. 56: (i) an agreement to do an act which at the time of the contract is impossible in itself: such an agreement is void; (ii) an agreement to do an act which, after the contract is made, becomes impossible or (by reason of some event which the promisor could not prevent), unlawful: such an agreement becomes void, when it so becomes impossible or unlawful; (iii) a third rule laid down by the sec. is that if, in such cases, the promisor knew or could have known with reasonable diligence that the act was impossible or unlawful, he must compensate the other party for the loss sustained by him through non-performance. Instances of the first case would be an agreement to discover a treasure by magic. "Impossible in itself" here means, impossible in the nature of things. Hence contracts which are impossible of performance because of non-existence of their subject-matter, do not fall under this sec. but under sec. 20.

Subsequent impossibility

The second rule deals with cases of subsequent or supervening impossibility. Where a contract, after it is entered into, becomes "impossible" of performance or becomes "unlawful", both parties are discharged from their obligation to perform it, as it thereby "becomes void". "Impossibility", however, has here a technical meaning. It may be caused in various ways:

(I) By the specific subject-matter of the contract being accidentally destroyed or failing to be produced: e.g. an agreement to let a musical hall for performance which however is subsequently destroyed by fire through an accident (*g*); an agreement to ship cargo by a specified ship in a fixed month, the ship suffering such injuries by stranding before the due date of shipment as to be unable to load the cargo (*h*). In both the cases, the contract would become void because of supervening impossibility of performance.

(II) Impossibility may also arise by reason of the foundation of the contract subsequently ceasing to exist. Thus in *Krell v. Henry* (1903), 2 K.B. 740, Henry having hired Krell's rooms to see the coronation procession of King Edward VII pass, was sued by Krell for the balance of the rent due. *Held*, Henry was not liable, as owing to the King's sudden illness, no procession had passed and the foundation of the contract therefore had totally failed.

Notice in this connection, however, that (i) difficulty in the performance of a contract owing to changed circumstances does not amount to "impossibility" under the sec. Thus where defendants in early 1914 had sold timber to the plaintiffs to be imported from Finland and to be delivered to the plaintiffs f.o.r. Hull, deliveries to commence in early July, and no deliveries being made till August, the defendants could not get timber from Finland owing to disorganisation of transport by reason of declaration of war, it was held that the contract was not dissolved, as what the rule contemplated was physical and not commercial impossibility of performance (*i*). Similarly, in a Bombay case (*j*), where a contract for freight was entered into to carry goods from Bombay to Amsterdam and owing to the declaration of war, freight to Amsterdam could only be procured on the due date at most exorbitant rates, it was held that the contract was not dissolved but that, on the contrary, the defendants had committed a breach of it, by not supplying the

(*g*) *Taylor v. Caldwell* (1862), 3 B. & S. 826.

(*h*) *Nickoll & Knight v. Ashton Eldridge & Co.* (1901), 2 K.B. 126.

(*i*) *Blackburn Bobbin Co. v. Allen* (1918), 1 K.B. 540.

(*j*) *Karl Etlinger v. Chhagandas & Co.*, 40 Bom. 301.

freight as agreed. Where goods are sold "subject to export licence", the fact that procuring export licence at the date of performance costs very much more to the seller than was anticipated when the contract was entered into, will not make the contract "impossible of performance" (k). Similarly (ii) the destruction of the state of peace, existing at the time of the contract, by a subsequent declaration of war, does not amount to destruction of the foundation of the contract. (iii) It has been further held that a state of insurrection in the State from where the goods are to be shipped and the prohibition by that State of the export of the particular article, does not amount to "impossibility of performance". Thus where a contract was entered into between two London Merchants for the sale and purchase of Algerian Esparto to be shipped by a French Company from an Algerian port and owing to an insurrection in that country, the French Government prohibited the collection and transport of the said goods from Algeria, it was held that the contract was not dissolved by subsequent "impossibility" (l). (iv) Stoppage of work by strikes is also not sufficient to make the contract void (m). If however (i) the subject-matter of the contract is confiscated by the State or (ii) requisitioned by the State, the contract does become void by becoming "impossible" of performance. Thus where under the orders of the Government, a large-scale engineering contract had to be suspended in order to direct labour to the production of munitions, it was held that the contract was dissolved and no breach was committed (n). (iii) Similarly, if contracts of the kind in question are prohibited by law, the contract becomes "impossible" and therefore void (see seq.).

(III) Frustration: Frustration of the adventure or the commercial object of the contract would also make the contract void.

Thus where a ship was chartered to load cargo at a certain port and carry it to Europe, and before she arrived there, there was a violent explosion of one of her boilers, which made it impossible for her to carry out her charter, it was held that the explosion frustrated the contract and that the parties were discharged from all liability (o). Similarly, where English sellers agreed to sell machinery to Polish buyers but before delivery was due, Poland was occupied by Germany, *held*, the contract was "frustrated" and the parties were discharged from their obligation thereunder (p). Where a theatre in which the defendant had agreed to screen the plaintiff's picture was pulled down under the orders of the Police, because it was in a dangerous condition, *held*, the contract was frustrated and the defendant was not liable to the plaintiff in damages (q). In England it has been held by a single Judge, that a compulsory purchase order by the Government does not put an end to a contract for sale of land on the ground of frustration (r). Scarcity of labour to fulfil a building contract has been held not to amount to frustration (r1).

This doctrine of frustration has been placed on various grounds: Sometimes it is said to depend on the presumed intention of the parties (s); sometimes it is regarded as depending on an implied term of the contract (t).

In a recent English case (u) the House of Lords placed the doctrine of frustration, not on principles of Justice and Equity or any extraordinary "absolving power" in the Court but on the ground of "just construction of the contract in accordance with an implication from the pronounced common intention of the parties". Lord Simon said, "The parties to an executory contract are often faced, in the course of carrying out, with a turn of events, which they did not at all anticipate—a wholly abnormal rise or fall in prices, a sudden depreciation of currency, an unexpected obstacle to execution

(k) *Braur & Co. Ltd. v. James Clerk Ltd.* (1952), 2 All E.R. 497.

(l) *Jacob Marcus & Co. v. Credit Lyonnais*, 12 Q.B.H. 589.

(m) *Hare v. Sec. of State*, 52 Bom. 142.

(n) *Metropolitan Water Board v. Dick Kerr & Co.* (1918), A.C. 119.

(o) *Joseph Constantine Line v. Imperial Smelting Corporation* (1942), A.C. 151.

(p) *Fibrosa etc. v. Fairbairn etc.* (1943), A.C. 32.

(q) *Narasu v. P. S. V. Iyer*, A.I.R. 1953 Mad. 300.

(r) *Hallington Estate Co. & Stonefield Estates Ltd.* (1952), 1 All E.R. 803.

(r1) *Davis Contractors v. Fercham Urban Council* (1956) 2 All E.R. 145.

(s) *Blackburn Bobbin Co. v. Allen & Sons* (1918), 2 K.B. 467.

(t) *Fibrosa's Case* (Supra).

(u) *British Movietone News v. London Cinemas* (1951), 2 All E.R. 617.

or the like. Yet this of itself does not affect the bargain they have made. If, on the other hand, a consideration of the terms of the contract, in the light of circumstances existing when it was made, shows that they never agreed to be bound in a fundamentally different situation which has now unexpectedly emerged, the contract ceases to bind at that point—not because the Court in its discretion thinks it just and reasonable to qualify the terms of the contract, but because *on its construction* it does not apply in that situation.”

The principle of this doctrine was examined by the Supreme Court in the recent case of *Satyabrata Ghose v. Mungniram* (1954), S.C.J.I. The Supreme Court pointed out that the principle of the doctrine, so far as Indian Law is concerned, is to be found and applied according to sec. 56 of the Contract Act. The doctrine in India does not rest on an “implied term” of the contract but merely on “the supervening impossibility or illegality” of the act agreed to be done. The “impossibility” need not be physical. Relief is given by the Court on the ground of subsequent impossibility when it finds that the whole purpose or basis of a contract has been frustrated by the intrusion or occurrence of an unexpected event or change of circumstances which was beyond what was contemplated by the parties at the time when they entered into the agreement. When an event or a change of circumstances occurs which is so fundamental as to be regarded by law as striking to the root of the contract as a whole, the Court will pronounce the contract to be frustrated and at an end. The Learned Judges further held that there was no reason why the doctrine of frustration should not apply in India to a contract for sale of land.

In the case in question, which was of a sale of a house site for development purposes, the Supreme Court held that looking at the actual existence of war conditions, when the contract was entered into, the extent of the work involved in the development scheme and the total absence of any definite period within which the work was to be completed, a requisition order by the Government as regards the land in question did not frustrate the contract.

Notice that in England the doctrine of frustration does not apply to demise of land (v). Even assuming it does, a tenant duly put into possession by the landlord, cannot invoke the doctrine on subsequent requisition of the premises by the Government, so as to escape liability for rent (w). In England, the question is now governed by a special Act, called the “Law Reform (Frustration Contracts) Act, 1943.

(IV) The last case is of personal incapacity in cases of contracts which require something to be performed in person, e.g. agreement by an artist to sing at a theatre, the artist being too ill to sing on the day fixed for performance (see ill. to sec.).

“Becomes Unlawful”

The reference here is to the effect of a declaration of war on subsisting contracts. War may affect contracts in a variety of ways: e.g. (i) by virtue of emergency legislation controlling prices or otherwise putting restrictions on trade; or (ii) by prohibiting or restraining intercourse with alien enemy.

Cases falling under the first class are those where, after a contract is made, Government by ordinance or otherwise, fixes the prices at which the

(v) *Matthey v. Curling* (1922), A.C. 180.
(w) *Sakhisona Dasi v. Gour Hari*, 56

C.W.N. 174. See also *Abdul Hassam v. Bala Hari*, A.I.R. (1952) Cal. 380.

articles in question should be bought or sold. In this connection, it has been held that if the contract price is higher than the control price of the article, the contract becomes void, as obviously, it cannot be performed in the way the parties intended. If the price fixed under the contract is less than the control price, the contract cannot be said to be impossible of performance, unless the Government notification also provides that the article shall not be sold below the controlled price. Other kinds of restrictions are also possible.

Thus in a Bombay case freight having been bought for the shipment of certain number of cotton bales from Bombay to Genoa on a certain ship, a subsequent Government notification prohibited export of cotton to Genoa. *Held*, contract became void (x).

The principle governing the second class of cases is: would the performance of the contract, when demanded after the termination of war, be the same as the parties intended or contemplated it should be, when they entered into the contract? If it is not, the contract is dissolved; if it can be, the contract is merely suspended, being capable of reviving when war conditions are over.

On this principle it has been held that unexecuted contracts of affreightment are always dissolved by a declaration of war (y); as also contracts of service. Similarly, where a contract for the purchase of steel bars was entered into between two Calcutta merchants, to be delivered "c.i.f.c.i. Free Hoogley" and the German ship carrying the goods was subsequently captured as Prize and taken to Ceylon, where the Prize Court condemned the ship but released the cargo, which arrived at Hoogley, under special arrangement, two years after the agreed time, it was held that the buyers were discharged under the contract, as the offered performance could in no sense be said to be the one intended under the original contract (z). A second test that is applied in this connection is, whether the carrying out of the contract involves trading with an alien enemy. If it does, the contract becomes void (a). Thus where a contract was entered into between two British subjects for sale of goods to be delivered to the buyer or his assigns in Hamburg, c.i.f., payment at Liverpool in exchange of shipping documents, and war being declared, the German ship, which was carrying the goods, put in at a neutral port, it was held that the contract was dissolved by the declaration of war and the buyer was not bound to accept the documents against payment of the price as the contract involved delivery to residents in enemy country (b). Similarly, in a Bombay case, where cargo was shipped from Hamburg to India, and war with Germany was subsequently declared, it was held that the buyer was not bound to take delivery, as it would involve trading with the enemy (c). Notice that on outbreak of war, a debt incurred before declaration of war is not abrogated but only the right to recover it is suspended (d).

Refund: Notice that under sec. 65, where a contract becomes void, person receiving any advantage thereunder, is bound to restore it to the other side. Thus if freight has been paid in advance and the contract of charter party becomes subsequently void under this sec., the ship-owner would be bound to return the freight to the charterer.

Reciprocal promises: one bad, the other good (secs. 57-58): The above secs. lay down two further rules with regard to reciprocal promises: (i) where persons reciprocally promise to perform certain things which are legal and under certain circumstances, other things which are illegal, the first set

(x) *Baggiano v. Arab Steamers Ltd.*, 42 Bom. 522.

(y) *Esposito v. Bowden*, 7 E. & B. 783.

(z) *Madhoram v. Sett*, 45 Cal. 28.

(a) *Re Badische Co. Ltd.* (1921), 2 Ch. 331.

(b) *Duncan Fox & Co. v. Bonka* (1915), 1 K.B. 365.

(c) *Nissim v. Haji Sultanali*, 40 Bom. 11.

(d) *Schering & Co. v. Stockholms Enskilda Bank* (1946), A.C. 219.

of promises are enforceable but the latter are not ; e.g. ordinary agreement of lease, with a promise to pay higher rent if used for gambling (ill. sec. 57). (ii) In case of alternative promises, one branch of which is legal and the other is not, the first is a contract, the latter is void (sec. 58), e.g. agreement to pay Rs. 1,000 in consideration of delivery of rice or smuggled opium (ill. sec. 57).

Appropriation of payments (secs. 59-61)

The above secs. deal with the important question as to how payments made by a debtor towards the discharge of several debts owed by him to the same creditor should be applied according to law. Three rules are laid down in this connection by the above secs. :

(i) When a debtor owing several distinct debts to the same creditor makes a payment, expressly or impliedly, indicating that it is to be applied in discharge of a particular debt, the creditor, if he accepts the same, is bound in law to appropriate that payment to that particular debt and no other (sec. 59). Thus if A owes B Rs. 1,000 and Rs. 2,000 on two promissory notes of different dates, a payment of Rs. 500 made by A to B towards part satisfaction of the first promissory note, if accepted by B, must be applied by B to the liquidation of that note only. If B is not willing to do so, he must, in law, return the amount back to A. In other words, the first right of appropriation is by law, given to the debtor. Note, however, that for the rule to apply the debts must be distinct. Thus the amount due on a mortgage, for principal, interest and costs constitutes one debt and not separate debts, one for principal and interest and the other for costs. A payment made towards principal of a debt, therefore, can be applied by the creditor towards the liquidation of the costs due (e).

(ii) Where the debtor omits to indicate, as to which of several debts, a particular payment is to be applied, and there are no circumstances from which such indication can be inferred, the creditor has the right, at his option, to apply the payment to any lawful debt due by the debtor to him, although his claim for such debt may be already barred by limitation (sec. 60). Thus if there are two mortgages, one carrying simple interest and the other compound interest with rests, the mortgagee receiving payment from the debtor, without any specific appropriation by the latter, is entitled to apply the same towards the discharge of the mortgage carrying simple interest in preference to the other mortgage (f). Notice that the creditor's right of appropriation is not confined to debts which are enforceable at law. He can appropriate the payment towards the discharge of a time-barred debt even. The debt, however, must not be an illegal debt. Secondly, the right of appropriation can be exercised by the creditor, at any time, even when filing a suit against the debtor for the balance of the amount due (g). Once exercised, however, the appropriation is binding on the creditor and cannot be subsequently altered by him to suit his convenience (h).

(iii) The third rule comes into operation where neither the debtor nor the creditor has made a specific allocation of a particular payment towards the discharge of a particular debt. In such a case the rule laid down is that the payments shall be applied in discharge of debts in order of time

(e) Jagannath v. Jhuma, 12 All. W.N. 645.

(f) Rameshwar v. Mahomed, 26 Cal. 37.

(g) Symore v. Pickett (1905), 1 K.B. 715.

(h) Rama Shah v. Lalchand, 42 Bom. L.R. 640.

and it makes no difference in this connection whether a particular debt is time-barred or not. If the debts are of equal standing, the payment shall be applied in discharge of debts proportionately (sec. 61). This rule (and sometimes the whole set of the above rules) is called the *Rule in Clayton's Case* (i). It is generally applicable in cases of running accounts between two parties, e.g. a banker and a customer, moneys being paid in and withdrawn from time to time from the account, without any specific indication as to which payment out was in respect of which payment in. In such a case, when final accounts, which may run over several years, are made up, debits and credits will be set off against one another in order of their dates, leaving only the final balance to be recovered from the debtor by the creditor.

In *Clayton's Case* (supra), one of the partners of a firm with which Clayton had an account died. The amount then due to Clayton was £1,717. The surviving partners, thereafter, paid out to Clayton more than that amount, while Clayton himself, on his part, made further deposits with the firm. On the firm being subsequently adjudged bankrupt, it was held that the estate of the deceased partner was not liable to Clayton, as the payments made by the surviving partners to Clayton must be regarded as completely discharging the liability of the firm to Clayton at the time of the particular partner's death.

The rule, of course, applies only when the creditor has not made any appropriation himself. There is one *exception* to this rule, however, which must be noted here. It is called the *Rule in Re Hellett's Estate*. The rule applies where a trustee mixes up trust funds with funds of his own. In such a case, if the trustee misappropriates any moneys belonging to the trust, the first amount so withdrawn by him will not be allocated to the discharge of trust moneys but towards the discharge of his own deposits, though such deposits were, in fact, made later in order of time. Thus if a trustee deposits Rs. 1,000 being trust money with a Bank and subsequently deposits Rs. 2,000 of his own in the same account, and thereafter withdraws from the Bank Rs. 1,000 which he misappropriates, the said withdrawal will not be debited against the trust amount of Rs. 1,000 according to the rule in Clayton's case, but only against his own deposit, though this was made later than the first deposit, thus leaving the trust fund intact. The rule is founded on principles of Equity.

Contracts which need not be performed (secs. 62-63)

The above secs. lay down the various other ways in which a contract can be discharged. A contract is discharged by performance (see ante). It is also discharged (i) where the parties agree to substitute a new contract in place of the old one; (ii) by the parties agreeing to rescind or (iii) alter the original contract (sec. 62); (iv) by the promisee remitting or dispensing with performance of the contract or a part of it; (v) by the promisee extending the time of performance of the contract or (vi) by his accepting any other satisfaction in place of its performance (sec. 63).

Novation

The first of these cases dealt with is called *Novation* or "*Novatio*". Where there being a contract in existence, some new contract is substituted for it, either between the same parties or between different parties, the consideration being the mutual discharge of the old contract, the transaction

is called "Novation". It thus includes two cases, viz. of a new contract between the same parties in place of the old one, e.g. where a promissory note is passed by the debtor to the creditor for the amount due on an account. It also includes a case where a new party is introduced and the old contract is varied by the liability thereunder being transferred to or being taken over by the new party, e.g. A being indebted to B for Rs. 1,000, a new agreement is arrived at, between A, B and C, under which, C agrees to take over A's liability to B, in consideration of B letting off A from his liability to B. In this connection, notice that an agreement between B and C to hold C liable in place of A does not discharge A's liability to B. Similarly, an agreement between A and C that C shall pay B the amount due by A to B does not discharge A's liability to B. In other words, a novation of the second type requires a tripartite agreement between A, B and C, under which B not only agrees to hold C liable in place of A but C must also agree to be liable to B in place of A (j). Whether there has been a "novation" in fact, is a question depending on the circumstances of each case.

Thus where one of the partners in a firm died, it was held that merely continuing to deal with the new firm after that knowledge did not operate as a discharge of the liability of the old firm (k). Where, however, a creditor, knowing of the death of a partner, transferred moneys from the current to the deposit account and took receipt from the surviving partners, it was held that his conduct amounted to an election to hold the new firm liable in place of the old (l).

What happens if the new contract which is entered into is not enforceable in law, e.g. for want of stamp or registration? The question depends upon the intention of the parties. If the new contract is intended by the parties to be in extinguishment of the old, the fact that the new contract is unenforceable at law, would leave the promisee without any remedy. On the other hand, when the new contract is merely incidental to the carrying out of the old contract, e.g. where a promissory note is given for value of goods bought or for moneys advanced, the original contract will remain enforceable, if the instrument constituting the "novation" turns out to be invalid for any reason (m). It has been recently held by the Privy Council that a novation whereby the single liability of one is converted into a joint liability of two on the basis of their entering into a partnership and being accepted as the debtors by the former creditor of one of them, is sufficient consideration for a promise by the other to pay the old debt of his partner (n).

Rescission

A contract can be rescinded by agreement between the parties at any time before its discharge by performance or otherwise. Thus a contract for sale of goods can be discharged by an agreement between the buyer and the seller, any time before delivery has taken place. The agreement for rescission may be either express or implied. Non-performance of a contract by both parties, for a long period, without complaint, may amount to an implied rescission. Rescission may be total or partial, i.e. the whole contract or some part or parts of it may be discharged by mutual consent. Where a contract is rescinded by the parties as above, notice that no compensation can be claimed by one party against the other, for the part already performed, in absence of a special stipulation to that effect (o).

(j) *Scarfe v. Jardine* (1882), 7 App. C. 345.

(k) *Re Head* (1893), 3 Ch. 426.

(l) *Re Head* (1894), 2 Ch. 236.

(m) *Krishnaji v. Rajmal*, 24 Bom. 360;

Pannalal v. Labhchand, A.I.R. (1955) Mad.

(n) *Gouri Dutt v. Madhoprasad*, 48 Cal. W.N. 36.

(o) *Lamburn v. Cruden* (1841), 2 M. & G. 253.

Alteration of contract

Where particular terms of an existing contract are varied by mutual consent, the contract as altered is the contract to be performed, the old contract being impliedly discharged thereby. In this connection the provision of sec. 92 of the Evidence Act must be noted. Under the sec., where the terms of a contract are reduced to writing, *no oral evidence* to contradict or vary its terms will be admitted in a Court of Law, except in certain specified cases. Assuming the alteration can be proved, it must be further shown that the alteration was accepted by the other party with full understanding of its meaning and effect. A material alteration made in a written contract by one party without the consent or authority of the other, may have the effect of making the whole contract void, e.g. where the date of a bond is altered by the creditor while it is in his custody (p), or where an additional signature is forged on a bond by a creditor (q), the rule is that the bond cannot be enforced by the creditor against the debtor even in its original shape. The principle is that a material alteration in a document by a party in whose custody it is, without the consent of the other party, will prevent the former from relying on the document, either as plaintiff or as defendant (r). It is otherwise with regard to documents creating interest in property, e.g. a mortgage deed. In this case, the document can be used for the establishment of the right originally created thereby (s).

Remission (sec. 63)

A contract is also discharged, if the other party remits or dispenses with its performance, e.g. a landlord accepts lesser amount as rent than the one originally agreed. Remission, however, requires a mutual agreement. No consideration is necessary in law to make a remission valid and binding. It is otherwise in English Law. An agreement to extend time also, does not require any consideration to make it effective. Notice, however, that mere forbearance to sue does not amount to extension of time. There must be an agreement to that effect (t).

Accord and Satisfaction

"Accepting any other satisfaction than the performance originally agreed", is called in English Law "accord and satisfaction". Thus if A owes B Rs. 5,000 and B accepts Rs. 1,000 from C in discharge of this claim against A, A is completely discharged from his old liability; similarly, an adjustment of account between two parties. The agreement to accept full satisfaction is called "accord"; the actual carrying out of the new agreement is called "satisfaction". "Accord" without "satisfaction" is no discharge of the contract (u).

Rules as regards restitution (secs. 64-65)

These secs. lay down the law as it stands in India, with regard to the duty of restitution, in cases of contracts which are subsequently avoided. Sec. 64 provides that where a voidable contract is rescinded by the person

(p) Govindsami v. Kuppasami, 12 Mad.

*399.
(q) Gogan Chandra v. Dhuronidhar, 7 Cal. 616.

(r) Suffell v. Bank of England, 9 Q.B.D. 555.

(s) Christacharlu v. Karibasaya, 9 Mad. 399.

(t) Anandram v. Bholaram, 47 Bom. L.R. 719.

(u) British Russian Gazette v. Associated Newspapers (1933), 2 K.B. 616.

entitled to do so, (i) the other party is discharged from his liability to perform a promise (if any) which he might have made and (ii) the party rescinding is bound to restore to the other party, any benefit he may have received thereunder. "Voidable" here is used in a general sense.

A contract may be "voidable" because (i) there was no free consent at its inception, e.g. under secs. 14-20 or (ii) by reason of default in performance, e.g. under secs. 39, 53, 54, 55, etc. The sec. applies to both the cases. Notice that a minor cannot be brought under the sec., the word "person" here being interpreted to mean a "person competent to contract" (v). Similarly, where an agreement entered into with the Governor-General was found to be void by reason of non-compliance with the formalities provided by sec. 175 of the Government of India Act, 1935, *held*, application of sec. was not excluded, there being no basic lack of capacity to enter into the agreement (w). Further, it is only a benefit received under the contract that has to be returned.

Thus if a purchaser of property deposits a sum with the vendor, with power to the latter to forfeit the same, if the purchaser fails to complete within the agreed time, the vendor is entitled in law to retain the deposit, on the contract subsequently going off by the purchaser's failure to complete as agreed (x). The sec. was invoked in an Allahabad case where a mortgage made by a guardian of a minor without the sanction of the court, was subsequently set aside, but only upon the terms of returning the moneys advanced under the mortgage (y).

Sec. 65 provides that when (1) an agreement is discovered to be void or (2) when a contract becomes void, any party who received any advantage thereunder is bound to restore it or to make compensation for it, to the other party. The sec. covers two classes of cases only: The first refers to agreements, which the parties, when they entered into them, honestly regarded as valid and binding, but which, for reasons subsequently discovered, cannot be enforced at law, e.g. an agreement to sell property which is inalienable, i.e. "Bhag" or "Narva" land (z). In such a case, the purchase money, if paid, must be returned to the purchaser, on the contract being found to be void. Similarly, in case of contracts which are void because of mutual mistake of both the parties under sec. 20, benefits (if any) received thereunder must be returned by one party to the other.

In a Bombay case a village Panchayat farmed out its right to collect taxes to the defendants. The contract was *ultra vires*, as the Panchayat had no such power. *Held*, under sec. 65, the Panchayat could recover the amount received by the defendant under the contract (a). In a recent case from Lucknow (b), the Privy Council held that where a mortgage deed, entered into during execution proceedings, without the sanction of the Collector, is aside as unenforceable, the case would fall under sec. 65, as of a contract "discovered to be void", and the mortgagee could recover under that sec. all the principal moneys and interest thereon at reasonable rates.

Notice in this connection, however, that the sec. does not cover contracts, the consideration for which is unlawful under secs. 23-24 of the Act (c). In such cases, the rule is that the money paid as consideration in respect of an executory contract which is illegal, can be recovered back on the transaction being subsequently repudiated, but if the illegal purpose or a material

(v) *Motilal v. Maniklal*, 45 Bom. 225;
Limbaji v. Rabi Ravji, 49 Bom. 576.

(w) *Union of India v. Ram Nagina Sing*,
89 C.L.J. 342.

(x) *Natesa v. Appavu*, 38 Mad. 178.

(y) *Bechu v. Bhabhuti Prasad*, 52 All.
831.

(z) *Jijibhai v. Nagji*, 11 Bom. L.R. 693.

(a) *Govind v. Yeshwant*, 43 Bom. L.R.
800.

(b) *Nisar Ahmad v. Mohan*, 43 Bom. L.R.
465.

(c) *Gulabchand v. Fulbai*, 33 Bom. 411.

part of it has been carried out, moneys paid cannot be recovered back, the maxim being "*in pari delicto malior est conditio possidentis*", which means that if both parties are equally guilty of a wrongful act, the law will help neither (d). Thus property fraudulently transferred by a person, in anticipation of insolvency, to his friends or relations, cannot be recovered back, if the purpose of such transfer has been accomplished, i.e. if the property has been successfully screened from the Official Assignee (e). It would be otherwise, however, if no insolvency supervened (f). The sec. also does not cover cases where, on a breach of contract occurring, the party in breach is disentitled to claim compensation from the other. Thus where a contract of insurance is avoided by the company on the ground of fraudulent misrepresentation by the assured, the premia already paid by the latter under the policy cannot be recovered back by him under the sec.

The sec. also covers cases of contracts "becoming void" by subsequent events, e.g. by subsequent impossibility or illegality under sec. 56. The illustrations to the sec. give the familiar case of a singer, under a seasonal contract of two months, who wilfully absents herself on the sixth night, which would entitle the theatre manager to rescind the whole contract. If the latter does so, the contract "becomes void" and he would be bound under the sec. to pay the artist for the five nights for which she sang. Notice that the law as laid down here is quite different from the English Law, under which, if a contract becomes void by reason of supervening impossibility or illegality, no right of compensation or return of benefits arises at all; the loss lying where it has already fallen (g). The Indian Law is otherwise, the section making a deliberate departure from English law as pointed out by the Privy Council in the recent case of *International Film Co. v. Murlidhar* (h). Sec. 66 deals with communication of recession of a contract and revocation thereof. The same principles apply to them as in case of proposals. Under sec. 67, if the promisee refuses or neglects to afford reasonable facilities to the promisor to perform his promise, the latter is discharged from his liability to perform the same.

CHAPTER V

QUASI CONTRACTS

What are Quasi Contracts? : Secs. 68-72 of the Act deal with, what are called in English Law "quasi contracts", i.e. certain types of transactions in which, there being in fact no "contract" between the parties, the Law, by a special rule, creates rights and obligations between them which are analogous or similar to those created by a "contract". The Chapter is described as "of certain relations resembling those created by contract" for this reason. The "quasi contracts" included are (i) a minor's liability to pay for necessities supplied to him (sec. 68); (ii) payment of money due by another (sec. 69); (iii) doing a non-gratuitous act for another (sec. 70); (iv) the case of a finder of goods (sec. 71); and (v) case of moneys paid by mistake or under coercion (sec. 72).

(d) *Taylor v. Bowers* (1876), 1 Q.B.D.

(e) *Petherpural v. Muniandi*, 35 I.A. 98.

(f) *Honapa v. Narsapa*, 23 Bom. 406.

(g) *Appleby v. Myers* (1867), L.R. 2 C.P. 651.

(h) 46 Bom. L.R. 178.

Necessaries supplied to a "minor" (sec. 68)

Under the sec., if a person incapable of entering into a contract (which would include both a minor and a lunatic) or anyone whom he is legally bound to support, is supplied by another with "necessaries" suited to his condition in life, such person is entitled to recover the value thereof from the property of such incapable person.

Two points must be noticed here : (i) The amount is recoverable only from the property (if any) of the incapable person and not from him personally. (ii) The objects supplied must be "*necessaries*".

The word "*necessaries*" is used here in a technical sense. It covers not only the bare necessities of existence, e.g. food, and clothes, but all things which are reasonably necessary to the minor, having regard to his station in life, e.g. a watch, a golf club, a bicycle may be included therein, but not articles of luxury or mere adornment : e.g. buttons are necessities but that would not include diamond or gold buttons. Recently, an engagement ring for one's fiancée has been held in England to be included under the term but not a vanity bag (i). In India, the term has been held to cover costs of defending a suit on behalf of a minor, where his property was in jeopardy (j), moneys advanced to a minor for the marriage expenses of himself and others whose marriages he was bound to perform, e.g. his sisters (k) and a loan to a minor to save his property from execution (l). Goods bought by a minor for purposes of trade, however, are not included in the term. Three conditions must be satisfied before things supplied to a minor can be called "*necessaries*" : (i) they must be suited to his condition in life ; (ii) they must be necessary for the minor's requirements when actually sold or delivered ; and (iii) the minor must not be already sufficiently supplied with them at the time. Thus where a minor Cambridge undergraduate bought eleven fancy waist-coats, when he was already well provided with clothing, *held*, that the trader could not recover the price thereof against the minor (m).

Payment of money due to another (sec. 69)

Sec. 69 and the next sec. are, in effect, exceptions to the rule that in order to amount to "*consideration*" the act, abstinence or promise constituting the same, must be given "*at the desire of the promisor*". When this is not so, the act, abstinence or promise does not amount to "*consideration*" and will not therefore support a "*contract*". Principles of equity, however, have created an obligation "*resembling contract*", where a person (1) who is interested in payment of money (2) which another is by law bound to pay, (3) pays the same to a third person. In such a case, the party making such voluntary payment is entitled in law to be reimbursed by the other (sec. 69); the principle being that the party benefiting by the payment must repay the amount paid for his benefit.

It will be seen that three conditions are necessary before the sec. can apply : (i) the person paying must be himself "*interested*" in making the

(i) *Elkington & Co. v. Amery* (1936), 2 All E.R. 86.

(j) *Watkins v. Dhunoo*, 7 Cal. 140.

(k) *Nardan Prasad v. Ajudhia Prasad*, 32 All. 325.

(l) *Kedarnath v. Ajudhia* (1883), Panj. Rec. No. 185.

(m) *Nash v. Inman* (1908), 2 K.B. 1.

payment. This is an important condition because if it were otherwise, every officious intervention in other people's affairs may create a legal liability.

Thus a sub-lessee paying rent due by the lessee to the landlord, in order to save the tenancy from forfeiture, would be entitled, under this sec. to recover from the lessee, the amount paid by him to the landlord, although there is no "contract" between the two (n). Similarly, where moneys are paid by a mother, to meet the marriage expenses of the daughters, she would be entitled to recover the same from the co-parceners under this sec. (o).

It has been held by the Privy Council (p) in this connection that for sec. 69 to apply it is not required that the person to be interested in the payment of money should at the same time have a legal proprietary interest in the property. The general purport of the sec. is clearly to afford a person who pays moneys in furtherance of some existing interest an indemnity in respect of the payment against any other persons who, rather than he, could have been liable at law to make the payment.

In this case certain mills were agreed to be sold by the trustees of debenture-holders of the mills to X. X thereafter entered into a contract of sale of the mills with Y. Municipal taxes payable by the debenture-holders with regard to the mills before their sale being outstanding, X called upon the trustees to pay the same but the latter sent no reply to X's request. X himself having also failed to pay the taxes, Y paid the same to prevent a forced sale of the mills as threatened by the Municipality. Held, Y was "interested" in the payment of the taxes and therefore could recover the amount from the trustees under sec. 69 of the Act.

The payment, however, must have been made *bona fide*, for the protection of one's own interest. Thus if moneys are paid by a squatter dishonestly, in order to create evidence of title in his favour, they cannot be recovered under the sec. (q). If both the parties are liable to pay, as in the case of co-sharers, a payment by one of the whole liability will be covered by the sec. according to the better opinion (r).

(ii) The other party must be liable to pay. This liability need not be statutory. It may be contractual also, but it must be there, otherwise the sec. will not apply. Thus where the assignee of a lease mortgaged his interest thereunder by way of sub-lease and the mortgagee sub-lessees, being in possession, failed to pay the rent under the original lease, it was held that a payment of the same by mortgagor could not be recovered by him from the sub-lessee mortgagees, as the latter were under no legal liability to pay the same (s).

Lastly (iii) the payment must be to a third party. Thus in a Madras case (t), certain lands were held by the Forest Department of the Madras Government, on a Mulgani (i.e. permanent) lease from the Mulgar (landlord). Arrears of rent being due by the latter to the Government, the same were paid up by the lessees (the Forest Department) to prevent a forced sale. Held, the payment could not be recovered under the sec. because it was a payment by Government to itself.

(n) Faizunnisa v. Bajrang, A.I.R. 1927, Oudh 609.

(o) Vaikuntam v. Kallapercram, 23 Mad. 512.

(p) Govindram v. Maharaja of Gondal, 53 Bom. L.R. 450.

(q) Desai Himatsingji v. Bhavabhai, 4 Bom. 643.

(r) Swarnamayi v. Hari Das, 6 C.W.N. 903.

(s) Bonner's Case (1898), 1 Q.B. 161.

(t) Sec. of State v. Fernandes, 30 Mad. 355.

Non-Gratuitous act for another's benefit (sec. 70)

The principle underlying the earlier sec., underlies sec. 70 also. Under the sec., where (i) a person *lawfully* does anything for another person or delivers anything to him, (ii) not intending to do so gratuitously and (iii) the other person enjoys the benefit thereof, the latter is bound to compensate the former in respect of the same. The sec. contemplates a class of cases where services are rendered by one person to another, without any express promise to pay for them. In such cases, if the benefit of the service is enjoyed by the person to whom it is rendered, he is bound to pay reasonably for the same.

Two conditions, however, are necessary to be fulfilled in such cases : (i) the services which are rendered must be non-gratuitous, i.e. they must be rendered with the intention of being paid for. Services freely rendered, without any expectation of a reward for them are not within the sec. Thus, saving another person's goods from a house on fire, will not bring the sec. into operation, if the act was the result of pure humanity or fellow-feeling ; but if the Salvage Corps of an Insurance Company with whom the premises are insured renders this service, the expectation being of payment of reward for services rendered, the case would fall under the sec. (ii) The second requirement is that the act must be, as the sec. says "lawfully done". This phrase has a technical meaning here. It means that the person doing the act must have a lawful interest in the doing of it (u). If he has no such interest, the case would fall outside the sec. In other words, the sec. does not justify officious interference with other peoples' affairs (v).

Thus a partner borrowing money on behalf of the partnership but without authority to do so, will make the partnership liable to repay the amount to the creditor, if the amount is actually used for partnership purposes. Similarly, directors of a company borrowing in excess of their powers, would make the company liable under similar circumstances. A joint tenant paying the rent to the landlord on behalf of both (w), and a co-sharer paying off the whole of the mortgage debt to prevent a threatened sale (x), are within the sec. Note however that co-heirs are not so entitled, as their interests are distinct and separate (y). Similarly, where the reversioners expectant on the death of a Hindu widow paid off her liabilities, it was held that they could not recover against the estate under the sec., as under Hindu Law, such persons have no interest at all in the estate while the widow is alive (z).

A payment made by a person for another against the latter's will, cannot be recovered under the sec. (a); so also a payment made by a person in wrongful possession, for his own benefit (b). A minor is not included under the term "another person" (c) because the word "person" has been held to mean "a person competent to contract" (Ibid).

In a recent Bombay case (d), a Municipality had entered into a contract with a firm of contractors to build a vegetable market for them within a fixed time. After the work was started, they further asked the same contractors to build a beef market and a slaughter house also, for them. The latter contract, however, was not in accordance

(u) Panchkore v. Hari Das, 21 C.W.N. 394.

(v) Damodar v. Sec. of State, 18 Mad. 88.

(w) Nirdosh v. Jakaria, 20 Cal. L.J. 492.

(x) Khairat v. Haidari Begum (1888), All. W.N. 10.

(y) Abdul Wahid v. Shaluka Bibi, 21 Cal. 496.

(z) Gopeshwar v. Brojo Sundari, 49 Cal. 470.

(a) Ram Tuhai v. Bisheswar Lal, 2 I.A. 131.

(b) Binda Koer v. Bhonda Das, 7 All. 660.

(c) Banke v. Mahendra, 19 Pat. 739.

(d) Pallonji Edulji & Sons v. Lonavla Municipality, 39 Bom. L.R. 835.

with the prescribed form. The contractors carried out the latter contract but failed to carry out the first within the stipulated time. On the Municipality refusing to pay the contractors, *held*, the contractors were entitled to claim payment for building the beef market and the slaughter house under sec. 70, though the contract with regard to them was not enforceable at law. In a recent Madras case, a Railway company had constructed a culvert near Madura which in 1938 it widened at considerable expense, on a requisition in that behalf being made by the Provincial Government. The company had done the work under protest, alleging that the order was illegal and that they would claim to recover the expenditure from the Government or the Madura Municipality or both. These two latter however had repudiated their liability. In a subsequent suit on behalf of the Railway Company against the Madura Municipality, it was held by the P.C. that sec. 70 could not be invoked to assist the Railway, for though the work was done lawfully and without intending to do it gratuitously, the defendants could not be made liable therefor, as it was not done for the defendants nor had the defendants enjoyed the benefit of it.

“Quantum Meruit”

The phrase means “payment in proportion to the amount of work done”. The doctrine is based on the same equitable principles on which sec. 70 is based. As Anson points out, the doctrine of “quantum meruit” comes into operation in three distinct cases: (i) Where a breach of contract occurs, of such a nature, as to discharge the whole contract, the party injured by the breach can recover against the other, proportionate compensation for the work already done under the contract under the doctrine of “quantum meruit”. Thus if A is engaged by B to write a series of articles for a magazine and if after the appearance of a few numbers, the magazine is abandoned, A can recover against B proportionate compensation for the work already published in addition to damages for breach of the rest of the contract (e). This case would probably fall under sec. 65 of the Act. (ii) In certain cases, Law will imply a contract or promise to pay for work done, e.g. in case of services rendered under a contract which is not enforceable on account of technical objection, e.g. the Statute of Frauds in England or want of Registration in India. Thus where C was employed as a managing director of a company under a written contract, but the contract was not binding on the company as the directors who made it, were not qualified, it was held that C could recover against the company for work done as managing director on the principle of “quantum meruit” (f). (iii) The conduct of parties may lead to an inference of a promise to pay reasonable remuneration; e.g. express or implied request to a person to render service, without specifying any particular remuneration for the same. This case is contemplated by sec. 70 of the Act. In all the above cases, the party benefiting by the services rendered is bound to pay “proportionate compensation” for the same, according to the doctrine of “quantum meruit”.

Finder of Goods (sec. 71)

Under the above sec., a person who finds the goods of another is placed under the same responsibility as a bailee. This is so, although there is, in fact, no contract of bailment between the two. For the duties of a bailee see secs. 151, 153-5 seq.; for the rights of the finder see secs. 168-9 seq.

(e) *Planche v. Colburn* (1831), 8 Bing. 14.

(f) *Craven Ellis v. Cannons Ltd.* (1936), 2 K.B. 403.

Moneys paid by mistake or under coercion (sec. 72)

Under the sec., a person to whom money has been paid or anything delivered by (i) mistake or (ii) under coercion, must repay or return it. The sec. is to be distinguished from sec. 21, which deals with mistake in the making of a contract. Under the sec., a debtor erroneously making an over-payment to the creditor is entitled to a refund (g). Notice that it has been recently held by the Privy Council (h) that sec. 72 is attracted once it is established that the payment made through mistake was not in fact due. It is irrelevant in this connection to consider whether there was a contract between the parties under which some other sum was due. The sec. applies to mistake of law as well as of fact and there is no inconsistency in this respect between sec. 72 and sec. 21.

It has thus been held that excess royalties paid under a mining lease under the mistaken belief that they were due, could be set off against royalties subsequently due (h). Similarly, it has been held in England that money paid by mistake of law by executors to a legatee Hospital are recoverable from the Hospital by an unpaid legatee though the Hospital may have spent the money (i). Where the mistake is caused by the fraud of a third person, the amount can be recovered (j). Where plaintiff pays tax at higher rate than that provided by Statute and sues for refund of excess on the ground of mistake, the suit is maintainable under s. 72 (j1).

Notice that "coercion" is used in the sec. in a more general sense than in sec. 15. It means "judicial or other compulsion". Thus if on execution of a decree, the property of a wrong party is attached and he pays the amount of the decree in order to raise the attachment, the payment would be under "coercion" and therefore recoverable under the section (k). Similarly, where excess charges are paid to Port or Railway authorities in order to clear goods which would otherwise be detained, the case would fall under the sec. Excess charges paid to Income-tax authorities under protest, would also be recoverable under the sec. Where sale tax was levied on articles which were not subject thereto, and subsequently the Court held the levy illegal, held, Government was bound to refund the tax as it must be deemed to have been paid under coercion (l).

CHAPTER VI**BREACH OF CONTRACT****Remedies in case of breach of contract**

When a contract is broken by a party, there are several courses of action which the other party may pursue: (i) He can refuse further performance of the contract; (ii) he can also resist a suit for specific performance. In these cases he acts as a defendant. As plaintiff, however, he has other courses open to him also: (i) He can bring an action for

(g) *Badrunnisa v. Muhamad Jan*, 2 All. 671.

(h) *Shri Shri Shibaprasad Sing v. Maharaja Shrish Chandra Nandi*, 54 C.W.N. 1.

(i) *Ministry of Health v. Simpson* (1950),

2 All. L.R. 1137 (H.L.).

(j) *Jones v. Warring & Gillow* (1926),

A.C. 670.

(j1) *Pannalal v. Union of India*, A.I.R. (1956) V.P. 26.

(k) *Kanhayalal v. National Bank of India*, 40 I.A. 76.

(l) *State of Vindya Pradesh v. Raghunath* A.I.R. 1952, V.P. 32.

specific performance or (ii) for injunction or (iii) for damages for breach of contract against the other party (iv) or for some or more of the above reliefs. (v) He can also sue to have it declared that the contract is no longer binding on him. Of these various remedies, only one, viz. of damages for breach, is treated by the Contract Act (secs. 73-74). The remedies by way of specific performance, injunction and declaration are dealt with by the Specific Relief Act.

Specific performance means the actual carrying out of the contract as agreed. The Court has power, under certain conditions, to compel a party to carry out his agreement in terms, instead of paying a money compensation or damages for its breach. The remedy of specific performance, however, is discretionary and will not generally be granted when (i) compensation in money is an adequate relief; (ii) when the Court cannot supervise the actual carrying out of the contract, e.g. a building contract or a contract of service, (iii) where the contract is in its nature revocable; (iv) or is made by trustees or corporations in excess of their powers (sec. 21, Specific Relief Act). Specific performance is usually granted with regard to contracts for sale of land and for taking of debentures in a company. In case of goods, it is granted only where the goods are of a special or unique kind, not easily available in the market.

Injunction is an order of a Court restraining a person from doing a particular act. It is given to enforce a negative stipulation in a contract, where damages would not be an adequate relief. The negative stipulation may be express or implied. An agreement to take all the electricity required for one's premises from a certain person implies an agreement not to take the same from any other person. A breach of such an agreement therefore could be restrained by injunction (m). A breach of a contract of personal service, however, will not be restrained by injunction, unless the negative stipulation is express (n). The remedy by way of injunction is governed by secs. 52-57 and that by way of *declaratory decree* is governed by secs. 35, 36, 42 and 43 of the Specific Relief Act.

Damages

"Damages" means the money compensation which the Court awards to a party against whom a contract is broken, in order to make good the loss caused to him by the breach. The fundamental principle underlying damages is not punishment but compensation. The law does not punish a party because he has broken a contract but if, by reason of his wrongful act, the other party has suffered any pecuniary loss, the Court will compel the party in breach to make good that loss by paying damages to the other party.

Damages are of various kinds. (i) *Nominal damages* are those which are awarded by a Court when it finds that though the defendant has been guilty of a breach of contract, the breach has not caused any appreciable loss to the plaintiff. In such a case the plaintiff is awarded nominal damages, e.g. in the shape of costs of the suit.

(ii) *Contemptuous damages* are awarded where the Court finds that though there has undoubtedly been a wrongful act on the part of the defen-

(m) Metropolitan Electric Supply Co. v. Ginder (1901), 2 Ch. 799.

(n) Whitewood Chemical Co. v. Hardman (1891), 2 Ch. 428.

dant, the wrong is of such a trifling or technical character, that no reasonably minded person would think of ventilating it before a Court of Law. In such cases the law gives contemptuous damages, e.g. a farthing or a rupee.

(iii) *Exemplary damages* are damages which are intended to show the Court's strong disapproval of the conduct of the defendant in committing the wrong. They are not proportioned to the actual pecuniary loss sustained by the party injured, but are inflicted by way of punishment, e.g. in case of breach of promise of marriage, defamation, etc.

(iv) Damages may also be (a) general or (b) special. *General damages* are those which are awarded as compensation for loss, naturally and in the usual course of events, resulting from the breach, e.g. on a breach of a contract of sale, the difference between the contract price and the market price on the date of breach. *Special damages* are those which, though flowing from the breach, are only incidentally so, but which are awarded by the Court, on the ground that they were in the contemplation of both the parties to the contract at the time they entered into it, e.g. loss of profit on an article of machinery arriving late. These are treated by sec. 73.

(v) Damages may be also (a) *liquidated* or (b) *unliquidated*. They are liquidated when the contract itself fixes a sum to be paid by one party to the other in case of breach. They are unliquidated, when they can only be ascertained by a decree of Court in a suit filed by one party against the other for breach of contract.

Measure of damage

The above phrase has two meanings in law : (i) It means the general principles according to which damage is to be calculated or assessed in any case of a breach of contract. (ii) It also means the actual quantum of damages awarded to a party in a particular case of breach of contract.

Rules as regards assessment of damages (sec. 73)

Four fundamental rules have been laid down by the Contract Act (sec. 73) in this connection. They are : (i) where a contract has been broken, the party suffering from the breach is entitled to receive, from the party who has committed the breach, compensation for any loss or damage caused to him thereby, *which naturally in the usual course of things arose from such breach*.

(ii) Such compensation is not recoverable for any remote or indirect loss or damage sustained by the party by reason of the breach.

(iii) Where a contract is broken, the party suffering from the breach is entitled to recover from the party in breach, compensation for any loss or damage which the parties knew, when they entered into the contract, as likely to result from such breach. The explanation to sec. 73, adds the fourth rule.

(iv) In estimating the loss or damage caused to a party by breach, the means which existed of remedying the inconvenience caused by the breach, must also be taken into account. Cl. (3) of the sec. lays down that the above rules are applicable to the breach of a quasi contract also.

Rule (i) above refers to general damages, rule (ii) to remote damages, rule (iii) to special damages and rule (iv) to the duty cast by law on the party suffering by the breach, to minimise the loss. The first three rules

were laid down in *Hadley v. Baxendale*, 4 H.C. 247, and therefore go by the name "*rule in Hadley v. Baxendale*".

General damages means that loss which, in the ordinary course naturally results from the breach. Thus on a contract for sale of goods, if the seller fails to give or the purchaser fails to take delivery, the loss which naturally results to either party from the breach is the difference between the contract price of the goods and market price of the goods *on the date of breach*. The result of granting damages on this basis is to put the parties in the same position as they would have been, if the contract had been carried out (o). Similarly, if A hires a passage by a boat to sail on a particular day, and the boat fails to sail on that day, the damages to which A is entitled to is the extra expenses (hotel accommodation, etc.) to which A is put to, by late starting of the boat. This is the loss which naturally, in the usual course of events, flows from the breach and hence it is awarded to A as general damages.

"Remote damages" is loss which does result from a breach, but which is so remotely connected with it that it cannot be called the *natural* consequence of a breach. Thus if A has to pay B Rs. 1,000 on a particular day and A failing to pay the same, B has to have recourse to insolvency, the loss resulting to B on account of being forced into insolvency is not the *natural* result of A's failure to pay Rs. 1,000. The loss which naturally, in the usual course of things, results from such a breach, is loss of interest, which B would have earned, if A had paid the amount at the agreed time [see ill. (n) to sec.]. Similarly, in the above case, the fact that by the late starting of the boat, A lost a profitable engagement at the port of destination is too remote a damage to be recoverable for a breach of an ordinary contract of passage [see also ill. (o), (p), (q) and (r) to sec.].

Special damages means loss resulting from a breach which the parties knew, when they entered into the contract, as likely to result from the breach. Given the above condition, the loss is recoverable at law, *although too remote*: Thus where A contracts to deliver to B a certain piece of machinery, which is necessary for B's mill (which mill is under a contract with Government, to A's knowledge), A's failure to deliver the machinery to B, will make A liable, not only for the extra costs (if any) incurred by B to get a substitute piece, but also for the *loss of profit* which B sustains by not being able to carry out the Government contract in question [see ill. (k) and (l) to sec.]. This loss is obviously too remote, but having been within the knowledge of the parties at the time of entering into the contract, A is liable for it under rule (iii), above.

Minimising damage: The fourth rule deals with the obligation which the law casts upon the *party suffering from the breach* to take reasonable steps to minimise the loss, resulting from the breach. Thus if A has undertaken to repair B's wall and A fails to repair it, B cannot sit inactive and see the whole wall collapse by rain and then claim the whole loss from A. The law requires B to take active steps to have the wall repaired by other means. If he does so and has to incur extra costs, he will be able to recover them from A. But if he does not do so, and the wall collapses, he cannot recover for the loss of the wall from A (p) (see seq.).

(o) Werthiem v. Chicoutimi Pulp Co. (1901), A.C. 301.

(p) Ramkumar v. Shankar (108), I.C. 433.

Special rules as regards damages

The illustrations to sec. 73 are important as they impliedly exemplify certain special rules with regard to assessment of damages: (i) The general rule as regards measure of damages in a contract for sale of goods, as is stated above, is the difference between the contract price and the *market price* on the date of breach. If there is no market price for the goods in question, however, the rule is to take the market price of the nearest substitute (q). If there is no nearest substitute the general rule followed is to take the cost price of the article at the place of origin and add to it conveyance charges, insurance (if usual), warehouse charges and the usual importer's profit, in order to find out the market price (r). (ii) Where time for performance has been fixed by the contract and the time, by *mutual agreement*, is extended by the parties, the damages will be the difference between the contract price and the price of the goods on such extended date (s). Note, however, that there must be an agreement to extend time. Mere unilateral extension of time does not come under the rule. (iii) If no time of performance has been fixed, the date when performance is asked for and refused is taken as the date of breach [see ill. (c)]. (iv) In case of late delivery, the difference in the market price between the due date and the actual date of delivery is taken as the measure of damages [see ill. (e)]. (v) If delivery is by instalments, due date of each instalment is taken as date of breach (t). (vi) In case of anticipatory breach, the date fixed for performance is taken as the date of the breach, though the contract may have been repudiated earlier (u). (vii) The cases of re-sales present peculiar features. When A sells goods to B which B then sells to C, a breach of contract by A will ordinarily make him liable for the difference between the contract price and the market price on the date the contract might have been performed and he will not be liable for B's loss of profit on his contract with C. A will not also be liable for damages (if any) which B may have to pay C [see ill. (j)], unless in both cases, A had notice of the subsequent contract (v). Further, if A contracts to deliver goods to B on a specified day when the price is Rs. 100 and he actually delivers it on a day when the price is Rs. 50, but B has, in the meanwhile, sold the article to C for Rs. 80, the measure of damage is the difference between Rs. 80 and Rs. 100, because that is the loss which B actually sustains (w). In a suit to recover damages for a breach of contract, under which the purchase price is pre-paid, the plaintiff is entitled to a return of the purchase price with interest upto judgment, as also the difference between the contract price and the market price prevailing at the date of a breach (x).

Warranty

Where goods are sold with a warranty and the same is broken, the seller is liable to pay all damages which his purchaser has to pay to the person to whom the goods are sold by him, whether the seller is aware of such a sale or not [see ill. (m)]. In an English case (y), furs were purchased by a wholesale furrier from A to make fur collars, as A was well aware of. He sold the fur collars to B, B to C and C to D, a draper, who sold them to a customer, who developed "fur dermatitis" because of bad quality of the fur. *Held*, A was liable for all damages and costs which the various intervening parties had to pay to their subsequent parties in suits brought by them against the former for damages for breach of warranty of quality. Similarly, where contracts were entered into for sale of cutlery, the sellers

(q) *Hende v. Liddell* (1875), L.R. 10 Q.B. 265.

(r) *Borris v. Huchenson* (1865), C.B.N.S. 445.

(s) *Ogle v. Earl Vane* (1868), L.R. 3 Q.B. 272.

(t) *Brown v. Muller* (1872), L.R. 7 Ex. 319.

(u) *Roper v. Johnson* (1873), 8 C.P. 167;

Najan v. Saleh Mahomed, 24 Bom. L.R. 998.

(w) *Hammond v. De Bussey* (1887), 20 Q.B.D. 79.

(x) *Werthiem v. Chicoutimi Pulp Co.* (Supra).

(y) *Rameshwar v. Paper Sales Ltd.*, 45 Bom. L.R. 906.

(v) *Kasler & Cohen v. Slavonski* (1928), 1 K.B. 78.

were held liable to indemnify their purchasers for all damages they may have to pay to their sub-purchasers for breach of warranty of quality (z).

“Minimising loss”

The duty cast upon the party suffering the breach to minimise the loss must be exercised by him reasonably and not extravagantly. Thus, to save an hour, it would not be reasonable to hire a special train. Similarly, if goods are not delivered at the stipulated time, the buyer cannot go into the market and buy at any or a reckless price. What is required is that he must take such natural and obvious steps to mitigate loss, as an ordinary prudent man would do in his own case. The “loss” here means, the actual loss at the date of breach. The fact that, by reason of the defendant’s breach, the plaintiff obtained another contract of value does not entitle the defendant to claim the benefit under this rule. Thus in *Jamal’s case* (a), shares were tendered by the seller to the buyer on the due date, which the buyer wrongfully rejected. The difference between the contract price and the market price at date of breach was Rs. 1 lakh and odd. The plaintiff subsequently sold the shares on a rising market and the loss was reduced to Rs. 79,000 and odd. *Held*, defendant was not entitled to the accretion in the price.

Contracts of immoveable property

A special rule obtains in England with regard to breach of contract for the sale of immoveable property. It is called the rule in *Bain v. Fothergill* (b), under which on such a breach occurring the seller in default is only liable to pay to the other (i) the earnest money (if any) deposited and (ii) the out-of-pocket expenses which might have been incurred. Exception is made only in case of (i) wilful default in giving possession; (ii) if the covenant for quiet enjoyment is broken; (iii) if the party had no title on the face of the agreement; and (iv) if there is failure on the part of the party to take steps in his power for clearing title. In such cases full damages are recoverable. In India it was once thought that the same rule operated. Now, however, it has been held (c) that this is not so, as sec. 73 makes no distinction between contracts for sale of goods and contracts for sale of land.

Interest as damages

Can interest be granted as damages? The question is not free from doubt. The better opinion is that as we have a special Act in India, viz. the Interest Act (XXII of 1839), which specially provides for cases where interest can be recovered, no interest can be granted as damages in cases falling outside the Act (see also sec. 61, Sale of Goods Act).

Penalty and liquidated damages (sec. 74)

Where a contract specifically provides that a certain sum shall be payable by one party to the other in case of breach, the question often arises whether the sum so fixed is “liquidated damages” or “penalty”.

(z) *Household Machines Ltd. v. Cosmos Exporters*, 62 T.L.R. 757.

(a) *Jamal v. Moola Dawood & Sons*, 43 I.A. 6.

(b) L.R. 7 H.L. 158.

(c) *Ranchod v. Manmohandas*, 32 Bom. 165.

"Liquidated damages" means that sum which has been fixed by the parties, as a genuine pre-estimate of the damage likely to be caused by the breach of the contract. The parties may wish to avoid the delay, cost and anxieties of a litigation and may, therefore, fix up between themselves, at the time of the contract, what approximately is the loss (if any) that is likely to be caused to one party or the other, on the contract being broken. Where a sum is fixed in such a manner and for such a purpose, it is called "liquidated damages". The general rule with regard to such damages is that the Court will not interfere with what the parties have already freely agreed to between themselves. On the other hand, the contract may contain a term, fixing the amount of damages payable by one party to the other in case of breach, which bears no relation to the actual or possible loss likely to result from the breach, but which is fixed "in terrorem", i.e. with the intention of "terrorising" the party into duly carrying out the contract. In such a case, the sum so fixed is called a "penalty" and the Court, being a court of "Equity and good conscience", will relieve against it, and will allow only such sum by way of damages as naturally results from the breach. English Law contains a variety of minute rules for distinguishing "liquidated damages" from "penalty". Sec. 74 of the Contract Act however makes a clean sweep of these rules and enacts, in its place, a simple rule, viz. that where a contract names any sum as being payable by one party to the other in case of breach, or if the contract contains any other stipulation by way of penalty, the party complaining of the breach is only entitled to recover "reasonable compensation, not exceeding the amount named or the penalty stipulated for", from the other party, if a breach occurs. The sec. further provides that a stipulation for payment of increased rate of interest may be a penalty. Exceptions however are made in cases of (i) a bail bond, (ii) a recognisance, and (iii) a bond given by person (in public employment) under the provisions of any law or under the order of the Government of India or of any local Government for performance of a public duty or act in which the public are interested. In these cases the whole amount fixed is payable, however excessive it may be.

Questions of "penalty" usually arise in case of bonds and other securities for money but they are by no means confined to such cases alone. Thus a contract between A and B that A will pay B Rs. 5,000 if A practises in Calcutta is a contract with a penalty clause [see ill. (b)]. Similarly, where F agreed to sing at K's theatre and conform to all its rules and it was agreed that each side should pay the other £1,000 as liquidated damages in case he committed any breach of its terms, it was held that the stipulation as to damages was by way of penalty (d). On the other hand, where the plaintiff was appointed the sole selling agent of the defendants to sell their cars in Yorkshire under an agreement, one of the terms whereof was that the plaintiff should deposit £300 with the defendants, which the defendants would be entitled to forfeit in case the plaintiff failed to pay the price of any car sold, it was held that the term as to forfeiture was not a penalty but liquidated damages and the defendants were entitled to retain the same (e). The question is always one of intention, to be ascertained after taking into consideration all circumstances of the case (e). In a case which came before the Privy Council from South Africa (f), the Government there had entered into a contract with a firm under which the firm was allowed to carry on in the Union, the business of diamond cutters on certain terms. One of the terms was that they should deposit £10,000 with the Government for the due carrying out of all the terms of the agreement. The Appellants guaranteed the payment of the said sum. On a breach occurring and on the firm becoming insolvent, held, the term as regards deposit (with power to forfeit) was in the

(d) *Kemble v. Farren* (1889), 2 Bing. 141.

(e) *Pye v. British Automobiles Ltd.* (1906), 1 K.B. 425.

(f) *Pearl Assurance Ltd. v. Govt. of U. of S. Africa* (1934), A.C. 570.

nature of a penalty and only the actual damage sustained could be recovered. Where a traveller on a tram belonging to the Bombay Municipality in order to escape a criminal prosecution paid down Rs. 5, being the fine payable under the Rules for travelling without a ticket, *held*, the fine was a penalty, and could be relieved against under sec. 74 (g).

The question whether a particular term in a contract is by way of penalty or liquidated damages is to be decided as at the date of the contract and having regard to its terms and not on the particular breach or breaches on which the claim is based (h). A "deposit" for due performance of a contract does not fall under sec. 74. It is in the nature of a guarantee for the due performance of the contract and is distinguished from "earnest moneys". On failure of performance, the promisee is entitled to forfeit such deposit amount and the wrong-doer cannot claim to recover the same under sec. 74 because that would be taking advantage of one's own wrong (i).

Thus where an agreement provided for a deposit for due performance of an agreement, e.g. to complete a conveyance, a clause, entitling the vendor to forfeit the sum in case of non-completion, is not a penalty clause, because it is introduced by way of security for the due performance of the contract (j). In a recent Madras case (k), on a hire purchase agreement for a Cinema projector, etc. the defendants were required to deposit with the plaintiffs a sum of Rs. 1,000 as security, with power to forfeit the same in case of breach. Default having occurred, the amount was forfeited by the plaintiffs. *Held*, neither sec. 64 nor sec. 74 of the Contract Act applied to the case, as the deposit was not by way of penalty and was in the circumstances, reasonable. Similarly, forfeiture of pay for failure to give notice is not within the sec. As the exception to sec. 74 specifically provides, amounts agreed to be paid as security for the due appearance before a Criminal Court (bail bond) or for the due appearance of a person under inquiry (recognisance) or a bond passed by a public officer appointed under any statute, local or central, for performance of a public duty, e.g. a bond passed by the Official Receiver or Official Assignee for duly carrying out the duties of their respective offices are payable in full, though they do contain penalty clauses. An administration bond and a bond passed under the Local Boards Act are not within the exception.

Every claim providing for forfeiture is not necessarily penal in character. The stipulation must appear "unconscionable" on a consideration of all the circumstances (k1).

A stipulation to pay a deposit as guarantee for due satisfaction of a contract is not to be regarded as a stipulation by way of liquidated damages, because the purpose of each is different. A deposit must also be distinguished from part payment made in discharge of contract. The former can be forfeited if such is the intention of parties, the latter must be taken in account (k1).

Interest by way of penalty

Bonds and other securities for money frequently provide for higher rates of interest in case a default is made in payment on the due date. The

(g) *Trikamdas v. Bombay Municipal Corporation*, 56 Bom. L.R. 264.

(h) *Dunlop Pneumatic Tyre Co. Ltd. v. New Garage Ltd.* (1915), A.C. 79.

(i) *Abba Gani v. Trustees of Port of Bombay*, 54 Bom. L.R. 273.

(j) *Panna Sing v. Arjan Sing*, 31 Bom. L.R. 909.

(k) *Subbarayulu v. Annamalai* (1944), 2 M.L.J. 74.

(k1) *Jagannadhaya v. Ramanath*, A.I.R. (1955) Orissa 11.

following rules in this connection may be noted: (i) If the stipulation for payment of higher rate of interest is from date of default, it is a question depending on the facts of each case whether it is a penalty or not. Where the original rate in a mortgage was Re. 1-12 and it was enhanced to Rs. 2 on a default, it was held not to be a penalty. Where 12 per cent interest was increased to 75 per cent on and from default, it was held otherwise. If the enhanced rate is from date of the bond or the security, it is always a penalty. (ii) Where compound interest is payable on default, if it is at the same rate, it is not a penalty; if it is at a higher rate, it is a penalty. (iii) Sometimes the provision is to pay interest on or after default. In such a case, the decision depends on the facts of each case. Thus where a promissory note, which provided payment by monthly instalments without interest, further provided that on failure to pay any one instalment, interest at 75 per cent would be charged, it was held that the clause was penal. In another case a bond stipulated for payment of interest at Re. 1 per cent per diem in case of default and the same result followed. (iv) Sometimes bonds provide for lower rate of interest, if amount is paid as agreed. This is unobjectionable. (v) The last case to consider is one of exorbitant rate of interest from date of bond, e.g. a bond for Rs. 500 advanced, with interest at 75 per cent. These cases are not under this sec., but may fall under the Usurious Loans Act of 1918, which generally allows relief only where (i) the rate of interest is excessive and (ii) the transaction appears to be substantially unfair.

Valid rescission of contract (sec. 75): Under sec. 75, whenever a person validly rescinds a contract, he is entitled to recover from the other party loss sustained by non-performance of the contract. The sec. is a corollary to secs. 39, 53, 55, 64 and 65 of the Act.

CHAPTER VII

INDEMNITY AND GUARANTEE

Contract of Indemnity defined (sec. 124)

Under sec. 124, a contract of indemnity is defined as "a contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself or by the conduct of any other person". The sec. is by no means exhaustive. It deals with only one particular kind of indemnity. In English Law, the term has a wide import and covers promises to keep the promisee harmless from loss caused by events or accidents over which nobody has any control, e.g. accident insurance and in fact, all types of insurance are contracts of indemnity. A contract of indemnity may arise either (i) by reason of an express promise or (ii) by operation of law, e.g. on a transfer of shares, the transferee, in law, undertakes to indemnify the transferor against all future calls. Similarly, where the promisor asks the promisee to do something for him, which is apparently legal but which on being carried out, causes wrongful injury to a third person, the law implies a promise on the part of the first party to indemnify the second, for all compensation which that party has to pay the third party for injury caused to him in carrying out the instructions of the first party (1).

(1) *Sheffield Corporation v. Barclay* (1905), A.C. 392.

Rights of indemnified when sued (sec. 125): Under sec. 125, the indemnity holder, when sued, has the following rights against the indemnifier. The indemnity holder, acting within the scope of his authority, is entitled to recover from the indemnifier, (i) all damages he may have to pay to a third party in respect of the matter for which the indemnity is given; (ii) all costs of suit which he may have to pay to such third party, if in bringing or defending the suit (a) he acted under the authority of the indemnifier or (b) if he did not act in contravention of the orders of the indemnifier and in such way as a prudent man would act in his own case and (iii) all sums paid by him on a compromise of such a suit, if, in so compromising, (a) he acted under the directions of the indemnifier or (b) as a prudent man would act in his own case and without contravening the orders of the indemnifier. The above rules follow logically from the very nature of the contract of indemnity.

Generally speaking, the judgment obtained by the third party against the party indemnified is conclusive against the indemnifier, though he is not a party thereto (*m*). As pointed out in a Bombay case (*n*), the sec. is by no means exhaustive of all the rights of an indemnity holder. It only deals with his rights in case of a suit against him. The question, when the right to claim indemnity arises, for instance, has not been treated at all. It has been held in this connection, both by the Calcutta and the Bombay High Courts, that the right to claim indemnity arises as soon as the indemnified has incurred an absolute liability. It is not necessary that he should have also discharged the liability before the claim to enforce the indemnity can arise (*o*). The only exception is where the indemnifier is himself interested in the payment of the money. In such a case, the indemnifier can be asked to pay the amount to the creditor (*ol*).

Rights of the indemnifier: The Act contains no mention of the rights which the indemnifier has, on carrying out his promise to indemnify. It has been held (*p*), however, that his rights, in such cases, are similar to the rights of a surety under sec. 141, i.e. he becomes entitled to the benefit of all the securities which the creditor has against the principal debtor, whether he was aware of them or not.

Contract of Guarantee defined (sec. 126)

Under the above sec., this is defined as "contract to perform the promise or discharge the liability of a third person, in case of his default". The person giving the guarantee is called the "surety", the person for whose default the guarantee is given is called the "principal debtor", and the person to whom the guarantee is given is called the "creditor". A guarantee may either be written or oral.

Indemnity and guarantee distinguished: These two kinds of contracts must be carefully distinguished from each other. A contract of indemnity differs from that of guarantee in the following points: (i) In the former, there are only two parties, in the latter there are at least three. (ii) In the former, the person giving the indemnity is primarily liable and there is no secondary liability. It is otherwise in the latter case, where there is both a

(*m*) Parker v. Lewes (1823), L.R. 10 Ch.

1035.

(*n*) Gajanan v. Moreshwar, 44 Bom. L.R.

703.

(*o*) Usman Jamal v. Gopal Purshotam, 56

Cal. 262.

(*ol*) Khettpal v. Madhukar Pictures, 57 Bom. L.R. 1122.

(*p*) Jaswant Singji v. Sec. of State, 14 Bom. 299.

primary and secondary liability of a sort. Thus if A and B go into a shop and A says to the shopkeeper "let B take what he wants, I shall see you paid", it is a contract of indemnity. On the other hand, if he says "I shall be responsible for the price", it is one of guarantee (q). (iii) In the former, the person giving the indemnity has some interest in the transaction, apart from the indemnity. In the latter, the guarantor is totally unconnected with the contract guaranteed except through the medium of his guarantee (r). (iv) In the former, there are generally two contracts, in the latter, there must be at least three. This was explained by the Court of Appeal in a recent Bombay case (s). The Court pointed out that to constitute a contract of guarantee under sec. 126, there must, first of all, be a contract between the principal debtor and the creditor, which lays the foundation for the whole transaction. Then there must be a contract between the surety and the creditor by which the surety guarantees the debt, the consideration for which contract, may move either from the creditor or from the principal debtor or both. The features, so far, are common to contract of indemnity and guarantee. In order to constitute a contract of guarantee, however, there must be a third contract, by which the principal debtor expressly or impliedly requests the surety to act as surety. Unless this element is present, there does not come into existence a contract of guarantee.

In the above case, the plaintiff had agreed with the defendant, who was a broker dealing in shares and securities, to act as his sub-broker. It was agreed between them that the plaintiff was to be responsible to the defendant for all business secured by him from his constituents and be answerable for due payment of all moneys payable by them with regard to their business. He also agreed to make good to the defendant all damage that may be caused to the defendant by reason of their default. Losses having occurred in respect of the plaintiff's constituents, the defendant settled the same by receiving smaller amounts from them. The plaintiff claimed that this discharged him from his liability as guarantor. *Held*, the contract was one of indemnity and not of guarantee, particularly as the constituents introduced by the plaintiff, not only did not know of the existence of the "guarantee" but were themselves not in existence, when the said undertaking was given. There is a further distinction in English Law which requires the contract of guarantee to be in writing in order to be valid, under the Statute of Frauds. This, however, is not so in India, where, as sec. 126 says, a guarantee may be either written or verbal.

Consideration for suretyship (sec. 127): Under this sec., anything done or any promise made by the creditor for the benefit of the principal debtor may be sufficient consideration for the surety to give the guarantee. Consideration, however, in some form, must exist, before a contract of guarantee can be valid. A guarantee gratuitously given cannot be enforced at law. A guarantee given in respect of a non-enforceable obligation, e.g. a time-barred debt, is not good. There must be an enforceable liability for which a guarantee is given before the guarantee can be effective (t). A surety who guarantees the performance of an agreement without consideration is not bound by his guarantee (u).

Liability of surety (sec. 128)

As sec. 128 lays down, the liability of the surety is co-extensive with that of the principal debtor, unless the contract otherwise provides. Thus

(q) *Birkmyr v. Darnell* (1704), 1 Sack. 27.

(r) *Sutton & Co. v. Grey* (1894), 1 Q.B.

285. (s) *Ranchod v. Shapurji*, 42 Bom. L.R.

550.

(t) *Mangu v. Shivappa*, 20 Bom. L.R.

447. (u) *Pestonji v. Meherbai*, 30 Bom. L.R.

1407.

if payment of a bill of exchange is guaranteed, the surety would ordinarily be liable, not only for the amount of the bill and interest thereon, but also for the notarial charges which may have been incurred for noting and protesting the bill. Notice that the question of a surety's liability depends primarily on the construction of the surety bond. A surety bond may create a personal liability of the surety as well as create a charge on his property as further security. It may, on the other hand, create a charge on his property only, without making the surety personally liable to the creditor (v). Further, a surety may guarantee the whole debt or a fraction thereof. In the latter case, two possibilities exist: he may guarantee the whole debt with a limit on his liability; or he may guarantee a limited amount of a floating debt, which may become due from time to time between the creditor and the debtor. If it is the former, he does not get the rights of contribution and subrogation (secs. 140, 145 and 146) till he has paid upto the whole amount of his limit. In the latter case, he secures the rights proportionately as and when he pays his proportion (w).

The surety's liability arises immediately the default of the guaranteed duty has taken place. The creditor is not bound to give notice of the default to the surety, unless it is expressly provided for, nor is the creditor bound to exhaust all his remedies against the principal debtor, before he can proceed against the surety (x). The surety, however, is entitled to have the liability of the principal debtor proved in the usual manner before he can be called upon to pay. The fact that the principal debtor has admitted the debt or that a judgment or award has been made against him for the debt does not bind the guarantor, unless of course, he was himself a party to the proceedings in which the judgment or award was given (y). The debt must be proved in the ordinary way, unless it can be shown that the guarantor has agreed to a particular method of proof, e.g. by production of account sales with regard to transaction on foreign exchange (y).

It has been recently held that a surety bond is to be strictly construed in favour of the surety. If there is any ambiguity therein, it must be construed in favour of the surety (z). The fact that the contract between the principal debtor and creditor is void or voidable, will not affect the surety's liability, e.g. if an advance to a minor is guaranteed, the surety would become primarily liable, on the minor's contract being discovered to be void (a). Notice that it has been held in Bombay that an acknowledgment of the debt or the payment of interest or principal, either by the surety or the principal debtor, will not have the effect of extending the period of limitation against the other (b). Calcutta in a recent case, however, has held differently (c).

Continuing guarantee (secs. 129-31)

This is defined by sec. 129 as "a guarantee which extends to a series of transactions". It is not confined to or exhausted by a single credit or transaction. Thus a guarantee given by A upto Rs. 5,000 for B duly accounting for rents collected, to C; A's guarantee of B's overdraft upto Rs. 5,000

(v) *Re Conley* (1938), 107 L.J. Ch. 257.
 (w) *Bardwell v. Lydall*, 7 Bing. 489.
 (x) *Sankana v. Virupaksha*, 7 Bom. 146.
 (y) *Shri Meenakshi Mills v. Ratilal Thakkar*, 48 Bom. L.R. 53.
 (z) *Pannaji v. Basappa*, 45 Bom. L.R.

510.

(a) *Kashiba v. Shripat*, 19 Bom. 697.

(b) *Gopal Daji v. Gopal Bin Sonu*, 28 Bom. 248.

(c) *Ranjit Roy v. Kishori Mohan*, 44 C.W.N. 985.

with a bank, are instances of continuing guarantees. Three peculiarities of such guarantees may be noted: (i) such guarantees are not exhausted by the first advance or credit or supply upto the pecuniary limit; (ii) they can always be revoked by notice to the creditor as to future transactions. This is expressly provided by sec. 130. Thus if A, in consideration of B discounting bills of exchange drawn by C, guarantees B for 12 months, the due payment of such bills, A can, after 3 months, by notice to B, revoke the guarantee, as regards all bills discounted thereafter, because it is a case of a continuing guarantee. Of course, A would remain liable for all bills discounted within the three months. Notice that it has been held in *Bombay (d)*, that the sec. does not apply to surety bonds for a minor required to be given to the Court when a guardian of a minor's property is appointed. Calcutta, however, has held otherwise (e). (iii) Death of the surety operates as a termination of a continuing guarantee as regards future transactions unless the contract provides otherwise (sec. 131). In the last two cases, an ordinary guarantee confined to a single transaction is not terminated. Whether a guarantee is a continuing guarantee is of course a question of fact. In a Bombay case the plaintiff stood surety for the lessee of a liquor shop, guaranteeing that the lessee of the shop would pay instalments due by him from time to time and bound himself accordingly. Some-time later, the plaintiff applied to Government for releasing him from his guarantee. *Held*, the guarantee was not a continuing guarantee and therefore could not be revoked by notice (f).

Joint debtors and suretyship (sec. 132)

Under this sec., where two persons jointly undertake a liability to a third person, e.g. sign a joint promissory note in favour of a Bank for an advance made to one of them, but as between themselves, one of them is a surety only for the other, the third party is not affected by the second contract, even though he may have knowledge thereof, unless he was himself a party thereto. In other words, the bank can, in the above case, recover the advance from the party who was in fact a surety in the transaction, as if he were the principal debtor himself. Notice however that when the third party is aware of the true position of the parties *inter se* he must not do anything which prejudices the rights or interest of the surety party under secs. 133-35. If he does, the surety party would certainly be discharged (g).

Discharge of surety (secs. 133-39)

The above secs. give the various cases in which a surety is discharged from his obligations as such. The principle underlying the rule is that the contract of suretyship is a peculiar type of contract. By such a contract a person takes upon himself the liability of carrying out another person's engagement. As such, the law watches very carefully that the surety is not called upon to perform any contract other than that which he himself guaranteed (h).

Several cases are envisaged: (i) Under sec. 133, any variance without surety's consent, in the terms of the contract, between the debtor and the creditor, discharges the surety as regards all transactions subsequent to the

(d) *Bai Sonu v. Ishwardas*, 19 Bom. 245.

(e) *Raj Narayan v. Fulkumari*, 29 Cal. 68.

(f) *Bhagandas v. Secy. of State*, 28 Bom. L.R. 662.

(g) *Overand Gurney Co. v. Oriental Financial Corporation* (1874), L.R. 7 H.L. 348.

(h) *Bonser v. Cox* (1844), 13 L.J. Ch. 260.

variance. Thus if A guarantees to B the payment by C of rent reserved under a lease, a subsequent agreement between B and C raising the rent, would discharge A from liability to C (i). Similarly, as illus. (b) to the sec. shows, a subsequent alteration of the terms of a contract, (without the surety's consent), by operation of law, e.g. by passing of a new statute, will also discharge a surety, even though the default guaranteed has occurred with regard to the unaltered terms of the contract. Where a person guarantees the due performance of a decree, a material alteration of the decree by the parties by mutual consent, without the consent of the surety, discharges the surety from his liability (j). Notice in this connection, that a plea that the alteration is nominal or of a minor nature or even beneficial to the surety, will not avail, as the law will not allow any judgment other than that of the surety himself, to decide as to what is more beneficial to him (k).

(ii) A surety is also discharged by any contract between the creditor and the debtor by which the latter is released, or by any act or omission on the part of the creditor, which has the effect of discharging the principal debtor (sec. 134). Thus the creditor accepting a compromise proposed by the debtor, will effectively discharge the surety, unless he expressly reserves his right as against him. Similarly, where payment of instalments under a hire purchase agreement was guaranteed, and on some instalments being in arrears, the owners terminated the agreement and seized the chattel, it was held that the surety was discharged from his liability (l). Notice however, that the bankruptcy of a debtor does not discharge the surety. Where the creditor reserves his right against the surety while discharging the debtor, the surety's right of indemnity against the debtor remains unaffected (m). It has been recently held by the Bombay High Court (n) that a scheme of arrangement under which creditors of a limited company in liquidation accept certain amounts of their claims in cash and the balance in shares of the company, has not the effect of discharging the sureties who have guaranteed the payment of the debts of the company, the scheme being regarded only as an alternative mode of liquidation, which the law allows the statutory majority of creditors to substitute for a pending winding up. Discharge of principal debtor by operation of law does not discharge the surety. Thus the fact that by operation of law, arrears of interest cannot be recovered from the principal debtor, does not prevent the creditor from recovering such interest from the surety, in case where such interest is otherwise recoverable (n1).

(iii) A contract between the creditor and the debtor to give time to or not to sue the debtor, also discharges the surety, unless he assents to the same (sec. 135). The rule applies also to a surety who is under no personal liability but has merely deposited documents (o). The result stated by the sec. does not follow if the creditor reserves his rights against the surety. Further, there must be a binding agreement to give time and not a mere giving of time. A nominal giving of time, which in fact accelerates the creditor's remedy against the principal debtor will not bring the sec. into

(i) *Khatun v. Abdulla*, 3 All. 9.
(j) *Bondru v. Dagdu*, 45 Bom. L.R. 438.

(k) *Pollak v. Everett*, 1 Q.B.D. 669.

(l) *Hewson v. Ricketts* (1894), 63 L.J. Q.B. 711.

(m) *Cole v. Lynn* (1942), 1 K.B. 142.

(n) *Ganeshram v. Shivnarayan*, 42 Bom. L.R. 451.

(n1) *Bank of India Ltd. v. Rustom*, 57 Bom. L.R. 850.

(o) *Jagjivandas v. King Hamilton & Co.*, 33 Bom. L.R. 709.

operation (p). Lastly, the contract of suretyship may itself provide that giving of time or accepting composition from the debtor, will not discharge the surety. In such a case again the surety is not discharged (q).

Notice that, as sec. 136 provides, an agreement to give time to the principal debtor entered into between the creditor and a third person does not discharge the surety. Similarly, as sec. 137 provides, a mere forbearance on the part of the creditor to sue the principal debtor or to enforce any remedy against him, does not discharge the surety, unless otherwise agreed. There was a controversy between some High Courts in India as to what the result would be, if the failure to sue the principal debtor extended over such a period that the creditor's remedy against the debtor becomes time-barred. This has now been set at rest by the Privy Council in *Mohant Sing v. U. Ba Yi* (r), where they held that a failure on the part of the creditor to sue the principal debtor with the result that the creditor's claim against him is time-barred, does not discharge the surety under sec. 135; similarly, an undertaking to give time or not to sue the principal debtor does not discharge the surety, when the creditor expressly reserves his rights against the surety.

In the above case, a building contractor had brought a suit against the trustees of a pagoda for work done on their behalf. The defendant who had guaranteed the performance of the contract by the trustees was also made a party. After suit, new trustees were appointed. Plaintiff therefore withdrew his suit against the old trustees (other defendants) and brought the new trustees on record. His claim against the new trustees was dismissed and not having withdrawn his suit against the old trustees with liberty to file a fresh suit against them, he was precluded from suing them again. *Held*, the defendant surety was not discharged because by keeping him as defendant throughout, the plaintiff had already reserved his claim against him. Notice, further, that the release of a co-surety by the creditor does not discharge the other surety nor does it free the surety so released from his liability to contribute to the other co-sureties (sec. 138).

(iv) A surety is also discharged, if the creditor does any act which is inconsistent with the right of the surety or omits to do an act which his duty to the surety requires him to do, and if the surety's eventual remedy against the principal debtor is thereby impaired (sec. 139).

Thus where a surety had guaranteed a debt payable by instalments, and one of the terms of the contract was that the decree-holder should issue such execution immediately a default occurred, it was held that a failure to issue such execution on a default occurring for such time that execution became time-barred, discharged the surety under the sec. (s). In an English case (t), a creditor omitted to register a security given for his debt as required by law, with the result that he became unsecured. *Held*, the surety was discharged by such omission. Similarly, where A had given a guarantee for B's fidelity to C on the understanding that C shall, once a month, personally check up the accounts, a failure to do so by C would discharge the surety under this sec. (see ill.). A creditor is not bound to insist upon particular kind of security from the principal debtor. It is only when he has taken such security, that the surety can claim the benefit of such security. If a creditor takes a security from the principal debtor, it is his duty to see that the security remains enforceable against the principal debtor and if any formalities are required by law in connection with the security, it would be his duty to see that such formalities are observed. But more than that, a creditor is under no obligation to do (tl).

(p) *Hulme v. Coles* (1827), 2 Sim. 12.

(q) *Greenwood v. Francis* (1899), 1 Q.B. 312.

(r) 43 Bom. L.R. 742.

(s) *Hazari v. Chunilal*, 8 All. 259.

(t) *Wulf v. Jay* (1872), L.R. 7 Q.B. 756.

(tl) *Bank of India v. Rustom*, 57 Bom. L.R. 850.

Notice that as observed by the Privy Council, a surety may also be discharged from liability as surety when the contract guaranteed by him is substituted by another one (not guaranteed by him), by reason of a new agreement between the parties. Thus where the original contract (guaranteed) was an advance of Rs. 1,25,000 on the security of four properties but the transaction actually put through was an advance of Rs. 1 lakh on three properties, *held*, the sureties were not liable, because in fact, they had not guaranteed the latter transaction (u).

Surety's right against the creditor (secs. 140-41)

A surety, in law, on becoming such, acquires rights, not only against the principal debtor, but also against the creditor. The latter rights are : (i) under sec. 140, according to which, a surety, after the guaranteed debt has become due or the default of the guaranteed duty has taken place, on payment or performance of all he is liable for, is invested with all the rights which the creditor had against the principal debtor. This is called *subrogation*. Thus if the creditor has the right to stop goods in transit or has a seller's lien, the surety, on payment of all he is liable for, will be entitled to exercise these rights (v). Notice that the right accrues to the surety only on payment in full of the whole of his liability. Payment in part will not be enough. If he is a surety for a whole debt with a limit on his liability, he will not be able to claim the right, till the whole debt has been paid. It would be otherwise when he is a surety of a part of the whole debt.

(ii) The surety, on such payment, becomes also entitled to the benefit of every security which the creditor has against the principal debtor, at the time the contract was entered into, whether the surety was aware of its existence or not. If the creditor by his negligence or default loses any such security, the surety is proportionately discharged. The surety, however, is not entitled to the benefit of any security subsequently given (sec. 141). Thus if a guaranteed advance is secured by a mortgage, the surety, on payment, becomes entitled to the mortgage security. Similarly, if moneys are raised on a mortgage of leasehold premises and a policy of insurance, the surety is entitled to claim from the creditor the assignment of both the securities, on payment of the amount guaranteed and the fact that on the same security the creditor had subsequently made further advances will not defeat his rights (w). It has been held in Bombay (x) in this connection, that a surety who has guaranteed a part of a debt, is not entitled to the benefit of the sec. till the whole debt is paid. Madras, however, has held otherwise (y), and there is English authority to the contrary also. (z). Notice that under English Law, the surety is also entitled to the benefit of securities subsequently given. This is not so under Indian Law.

Certain other rights which a surety also enjoys against the creditor may be mentioned here : (iii) The surety has a right, any time before the guaranteed debt has become due and before he is called upon to pay, to require the creditor to sue for and recover the guaranteed debt (a). This is

(u) *Pratapsing v. Keshavlal*, 37 Bom. L.R. 315.

(v) *Imperial Bank v. London & St. Katherine Docks* (1877), 5 Ch.D. 195.

(w) *Forbes v. Jackson* (1882), 19 Ch.D. 615.

(x) *Gordhandas v. Bank of Bengal*, 15 Bom. 48.

(y) *Bhushaya v. Surya* (1944), 1 M.L.J. 1.

(z) *Goodwin v. Grey* (1874), 2 W.R. 312.

(a) *Rouse v. Bradford Banking Corp.* (1894), 2 Ch. 70.

called the right to file a *quia timet* action against the debtor. In such a case, however, the surety must undertake to indemnify the creditor, for the risk, delay and expense which he may incur by so doing. (iv) Lastly, the surety is entitled, on being sued by the creditor, to rely on any set-off or counter-claim, which the debtor might possess against the creditor.

Guarantee when void (secs. 142-44)

Guarantee is not a contract *uberrima fide* (of abundant confidence) and the creditor generally is not bound, at his peril, to make a full disclosure of all material facts to the surety before entering into the contract, nor for the matter of that, is the principal debtor bound to do so. Thus where a guarantee is given to a Bank, it is not obligatory on the bank to inform the intending guarantor about all matters affecting the debtor's credit or any matter which makes the transaction more hazardous (b).

There are certain cases, however, where a guarantee is invalid. Thus (i) where a guarantee has been obtained by means of misrepresentation made by the creditor, or with his knowledge or assent, as to a material part of the transaction, the guarantee is void (sec. 142).

(ii) Where a guarantee has been obtained by means of keeping silence as to a material circumstance, it is invalid (sec. 143). "Keeping silence" here means intentional concealment of a material fact, as distinguished from a mere non-disclosure thereof (c). Some element of fraud must exist (c). Thus where A gives a guarantee to B for C's duly accounting for his receipts, a failure on the part of B to disclose to A the fact of a previous defalcation by C would come under the sec. (see ill.). Similarly a secret additional agreement between the creditor and the principal debtor, which materially affects the debtor's liability to make default but which is concealed from the surety, will make the guarantee void (see ill.). A contract of guarantee is not a contract "*uberrima fide*" but is a contract "*strictissima juris*", or a contract which must be strictly performed. An employer of a servant therefore commits no default as regards the guarantor, if he continues to employ, without a notice to the guarantor, a servant whose honesty is suspected but not disproved. It would be otherwise if the servant's dishonesty was proved (c1).

(iii) Similarly, where a contract of guarantee is entered into on condition that the creditor shall not act upon it until another has joined as co-surety, the contract is void, if the other party fails to join (sec. 144).

Surety's rights against the principal debtor (sec. 145)

The surety has rights against the principal debtor also. The most important is (i) the right of indemnity. As the sec. says, in every contract of guarantee, there is an implied promise by the principal debtor to indemnify the surety. The surety is entitled to recover from the debtor all sums which he has rightfully paid under the guarantee but not any sum wrongfully paid. Notice that the right occurs only on payment by the surety of all that he is liable for under the guarantee. If the surety discharges the liability by payment of a lesser sum than the one originally due, he can only recover the lesser sum from the debtor under the sec.

(b) Wythes v. Labouchere (1859), 3 De. G. & J. 598.

(c) Balkrishna v. Bank of Bengal, 15

Bom. 585.

(c1) Radhakant v. United Bank of India, A.I.R. (1955) Cal. 217.

The other rights which a surety enjoys against the principal debtor are (ii) a right to file a *quia timet* action or an action before payment, to compel the debtor to pay off the liability guaranteed. This can be done only if and when the debt has become an ascertained debt and further, if there is a present liability to pay on behalf of the guarantor (d). (iii) The surety has also the right to issue a third party notice against the debtor when sued by the creditor.

Co-sureties (secs. 141-42)

The above secs. lay down the rules with regard to the liability of co-sureties. (i) Under sec. 141, where two or more persons are co-sureties for the same debt or duty, either jointly or severally and whether under the same or different contracts and whether with or without the knowledge of each other, each co-surety, in absence of a contract to the contrary, is liable, as between himself and the other co-surety, for an equal share of the whole debt or of the part of it which remains unpaid. Thus if A's house is insured against fire with two insurance companies for a certain amount, and the house is totally destroyed, each underwriter is bound to contribute equally with the other in making up the loss. Similarly, if A, B and C have guaranteed to D the payment by E of Rs. 3,000, they are each bound to contribute Rs. 1,000 to make up Rs. 3,000, in case E makes default (see ill.). Notice that the rights defined by the sec. are available to co-sureties amongst themselves only. The creditor can, at his choice, recover the whole debt from any one of the co-sureties. A surety, however, who pays more than his share is entitled to contribution from his co-sureties. All co-sureties are also entitled to the benefit of any security which any one of them may have obtained from the principal debtor, whether they were aware of it or not. Where one surety has paid more than his proportionate share, the proper procedure is for him to file a suit for contribution against his co-surety, making the principal debtor also a party thereto. His right to file such suit is not affected by the fact that a security held by the plaintiff has not been realised, the co-surety's right being to share proportionately in the proceeds thereof when realised (e). Notice, further, that there is no right of contribution between co-sureties *inter se*, when the sureties have guaranteed different parts of the same debt, e.g. under a Lloyd's policy. In such a case, each is liable to pay the whole portion which he has guaranteed.

(ii) Where co-sureties are bound in different sums with reference to the same debt, they are liable to pay equally, so far as the limit of the respective obligations go (sec. 142). Thus if A gives a guarantee upto Rs. 10,000, B upto Rs. 20,000 and C upto Rs. 30,000, with regard to D duly accounting for his receipts as agent for E, the respective liabilities of A, B and C, on a default of Rs. 60,000 occurring, would be A Rs. 10,000, B Rs. 20,000 and C Rs. 30,000. In other words, in such a case, there cannot be an equality of contribution.

(d) *Morrison v. Barking Chemical Co.*
(1919), 2 Ch. 325.

(e) *Kamal Chander v. Sushilabala*, 42
C.W.N. 1258.

CHAPTER VIII

BAILMENT

Bailment defined (sec. 148): Bailment is defined by sec. 148 as "the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned, or otherwise disposed of, according to the directions of the person delivering them". The person delivering the goods is called the "bailor", the person to whom goods are delivered as above is called the "bailee". The explanation points out that delivery of possession is not necessary, where one person already in possession of goods, contracts to hold them as 'bailee'. The consideration for the contract of bailment is the bailor's parting with the possession of the goods. The transfer of possession may be actual or constructive, e.g. where A holding goods on behalf of B, agrees to hold them on behalf of C, to whom A has sold the goods. "Possession" here means "juridical possession". The possession of a servant is not juridical possession but bare custody. Such a person, therefore, does not fall within the definition of a "bailee".

Common instances of bailment are : giving cloth to the tailor to make a coat, delivering a car to repairers for repairs, consigning goods to a commission agent for sale, delivering goods to a railway company for carriage. Notice that delivery to the bailee can be made by anything which has the effect of putting the goods in the possession of the bailee or of any person on his behalf (sec. 149). Bailment must be distinguished from hiring. Generally the intention behind an ordinary bailment is to transfer possession of the goods to the bailee, with a view to their safe keeping. The bailee generally does not and in fact is not entitled to use the goods for his own purposes. Hiring is the bailment of goods for reward, with liberty to the hirer to use the goods for his own purposes in terms of the contract of hire.

Duties of bailor (sec. 150)

Under sec. 150, (i) the bailor is bound to disclose to the bailee all faults in the goods bailed of which the bailor is aware and which materially interfere with the use of them or which expose the bailee to extraordinary risks. If he fails to do so, he is liable to the bailee in damages.

(ii) Where goods are bailed by way of hire, the bailor is liable to make good loss caused to the bailee by such defects, whether he was aware of their existence or not. Notice that there is a difference in the degree of responsibility of the bailor, according as the bailment is gratuitous or non-gratuitous. In the first case, the bailor is liable only for known defects, in the latter case, he is liable also for unknown defects. Thus if A lends his horse to B for riding and the horse is vicious to the knowledge of A, A is bound to disclose the fact to B. Similarly, if a carriage is hired by A from B and the carriage has a defect which makes it dangerous to ride, B is liable to A for damage caused to A by such defects, and this whether B was aware of the defect or not (f). In other words, where an article is hired out for use there is an implied warranty that it is fit for such use. If there is a breach of this warranty, there is no obligation to pay the hire (g).

(f) *Hyman v. Nye* (1881), 6 Q.B.D. 685.

(g) *Isufali v. Ebrahim*, 23 Bom. L.R. 403.

Duties of a bailee

Duty to take care (sec. 151): The first and foremost duty of a bailee is to take care of the goods bailed with him. The extent of this duty is defined by sec. 151. Under the sec., a bailee, in absence of a contract to the contrary, is bound to take as much care of the goods bailed, as a man of ordinary prudence would do of his own goods, of equal quality, bulk and value. In other words, he is bound to take the ordinary prudent man's care of the goods bailed and if loss occurs in spite of such care, the bailee is not liable for the loss (sec. 152).

Thus if an article bailed is kept unlocked by the bailee, while he locks up similar articles of his own, the bailee will be liable for the loss (h). Similarly, if a servant of the bailee commits a theft of the article bailed and the bailee has been negligent in the selection of the servant, the bailee will be liable (i). It would be otherwise, if there was no negligence in the selection of the servant. Want of skill usually associated with a particular class of work, would be evidence of negligence (j). Notice that where goods are bailed with another, the latter has no right to place the goods in the custody of a third person without the bailor's authority. If he does so he commits a breach of his contract with the bailor and is liable for all damages caused to the goods while in custody of the third person (k). In a recent English case a Railway Company had received certain baggage from A in their cloak room and had issued tickets in respect thereof to A. Subsequently, through the negligence of their clerk, the baggage was allowed to be removed by B, who had produced no ticket and who had given no satisfactory proof of loss of the tickets. One of the terms of the contract provided that the company will not be liable for mis-delivery or for articles exceeding £5 in value if their value was not previously declared. A had not made such declaration. *Held*, the company was liable, because it had broken the fundamental terms of the contract, viz. that the Company would deliver the articles to the person producing the ticket or in case of loss of the ticket, to the person satisfactorily proving the ownership of the articles; that such being the case, the whole contract was terminated and therefore the rule as regards declaration of value ceased to be operative (l). Notice that the sec. makes no difference between a gratuitous and a non-gratuitous bailment with regard to this duty to take care.

EXEMPTION CLAUSES: Contracts of bailment, sometimes contain exemption clauses, exempting bailees, e.g. warehousemen, from liability for negligence. The rule in such cases is that if the negligence occurs on the part of the bailee while carrying out the terms of the contract, the clause will protect him (11). But if the bailee has deviated from the contract or has been in breach of a fundamental term of the contract of bailment, such a clause will not protect him (12). Thus a clause in a hire purchase agreement for a motor car, excluding warranty of fitness, condition, age or road worthiness, was held not sufficient to protect the vendor, where the car, when delivered, would not go (13). A term in a contract that goods bailed are at "owner's risk" does not absolve the bailee from liability in case of loss, unless they prove that loss was caused by some cause, not involving their negligence or that loss was caused by their negligence. In such cases, the clause would protect the bailees but not otherwise (14).

Care required of "common carriers"

A question of some difficulty arises with regard to the standard of care which is required by law from a "common carrier". According to English

(h) *Clarke v. Earnshaw* (1818), Gow, 30.

(i) *Williams v. Curzon Syndicate* (1919), 35 T.L.R. 475.

(j) *Wilson v. Brett* (1843), 11 M. & W. 113.

(k) *Edwards v. Newlands* (1950), 1 All E.R. 1072.

(l) *Alexander v. Railway Executive* (1951), 2 All E.R. 442.

(11) *Spurling Ltd. v. Brawdshaw* (1956), 2 All E.R. 121.

(12) *Bontex Knitting Works v. St. John's Garage* (2) (1944), 1 All E.R. 381.

(13) *Karsalis v. Wallis* (1956), 2 All E.R. 866.

(14) *Woolmer v. Delmere Price Ltd.* (1955), 1 All E.R. 377.

Common Law the liability of a "common carrier" and "innkeeper", with regard to taking care of goods bailed with them by their customers, is absolute. In other words, they are liable for all loss caused to the goods bailed with them, as if they were insurers of the goods, except when the loss is caused by an act of God or by the King's Enemies. Thus taking due and proper care of the goods bailed, as a prudent man would take in his own case, would not absolve them from liability for the loss.

A "common carrier" is one who holds himself out as ready for hire for transport of goods of all persons indifferently, from one place to another, by land, sea or air, for reward. He must do his work as a business and not as a casual occupation. The duty of such a "common carrier" is to carry all goods offered to him for transport by persons willing to pay his hire, provided (i) there is available room in his vehicle; (ii) the goods offered are of the usual kind carried by him; and (iii) the destination is also one to which he usually carries goods. If a "common carrier" wrongly refuses to accept goods, he is liable to be criminally indicted and will also be liable in damages.

In India, these rules of English Common Law were followed for some time. But in 1865 the Carriers Act was passed and thereafter the Railways Act of 1890, the Carriage of Goods by Sea Act of 1925 and the Carriage by Air Act of 1934 were passed by the Indian Legislature and the question therefore is now governed by the respective provisions of these Acts. The Carriers Act of 1865 defines a "common carrier" as "a person, other than Government, engaged in the business of transporting for hire, property from place to place by land or inland navigation, for all persons indiscriminately (sec. 2). A "common carrier", under the above definition, would not include a carrier of passengers, railways under the control of Government and owners of sea-going merchant ships. Under the Act, no "common carrier" is liable for loss or damage to specific kinds of property shown in the schedule, e.g. gold, silver, precious stones and jewellery, and such other property of special value, exceeding Rs. 100 in value, unless its value and description are properly declared beforehand (sec. 3). He can also, by a special contract, limit his liability in any particular way (sec. 6). But in no case can a "carrier", by a special contract, escape liability for the following: (i) with regard to property for which such a declaration has been made, the "common carrier" is liable for all loss or damage caused to it by the negligence of the carrier or any of his agents or servants; (ii) he is also liable with regard to all property carried by him, whether declared or not, for loss caused to it by the criminal act of the carrier or any of his agents or servants (sec. 8). Further, the burden of proving that loss or damage to the goods was not caused by the negligence or criminal act of the carrier or his agents is primarily on the carrier (sec. 9). The carrier, however, shall not be liable for any loss unless notice in writing of the loss or damage has been given to him before suit and within 6 months of the loss or damage coming to the knowledge of the plaintiffs (sec. 10).

The question whether the general principles of English Law as regards the "common carriers" applied to "common carriers" under the Act, has been answered by the Privy Council in the affirmative (*m*), with the result that the law as to "common carriers", coming under the Act of 1865, is to

be construed according to the principles of English Common Law as modified by the Carriers Act and not according to secs. 151 and 152 of the Act.

Carriers by sea: They are not within the Act of 1865. According to the Calcutta High Court the question of their liability is governed by secs. 151 and 152 of the Contract Act (n), while the Madras High Court has held that their liability is governed by the English Common Law rules applicable to "common carriers" (o). Under the Carriage of Goods by Sea Act of 1925, any term in a contract of carriage exempting the carrier or the ship from liability for loss or damage to goods, from negligence or from any default or failure to discharge duties cast upon them by the Act shall be null and void. Further, no carrier or ship shall be responsible for loss or damage to goods exceeding Rs. 100 per package in value unless the nature and value of the goods have been declared by the shipper before shipment and are inserted in the bill of lading. Apart from the above, the contract of affreightment may contain any special terms. These are some of the rules adopted by the Act from the Brussels Convention on Maritime Law.

Carriers by Railway: The liability of Railway Administration for negligence is determined by the Railways Act of 1890. Under sec. 72 of that Act, a railway company's responsibility for taking care of goods bailed with them is governed by secs. 151-52 of the Contract Act and not by the special rules of English Common Law. It is, therefore, not liable for loss of goods if it has taken as much care of the goods bailed, as an ordinary prudent man would take of his own goods. By another sec., however, the railway companies are given power to enter into special contracts, modifying their above liability. These contracts must be in special forms and must be sanctioned by the Central Government. These are the various "Risk Notes" (from A to E), under which goods can be consigned on a railway, at "owner's risk", "Railway's Risk" or at "specially induced rates", as the case may be. Under these "risk notes" the railway company stipulates that it will not be liable for loss or damage to goods at all or will be liable for the same only in certain special cases.

Carriers by air: Under the Carriage by Air Act of 1934, a carrier by air is liable for all damage or loss of goods if the occurrence which caused the loss took place during carriage by air. The carrier, however, will not be liable if he proves that he and his agents had taken all necessary measures to avoid the damage or that it was impossible to take such measures. Contributory negligence of the injured person will exonerate the carrier from liability. In case of goods, the liability of the carrier is limited to 250 francs per kilogram only, unless the passenger has made a special declaration at the time of handing over the package. These are some of the rules adopted by India from the Warsaw Convention. A carrier by air can limit his liability as regards his duty to take care of passenger, by means of such terms as are reasonable. This is quite different from his duty to carry all and sundry according to his profession. In this respect there is no distinction between a common carrier and a private carrier (p).

Innkeeper

A "common innkeeper" in English Law is one who keeps an inn for reception of travellers. He is bound to receive all travellers who resort to

(n) *Mackillican v. Compaigne des Messageris*, 6 Cal. 227.

(o) *Haji Ishmail v. Compaigne des Mes-*

sageris, 28 Mad. 400.

(p) *Alfred Luddet v. Ginger*, 51 C.W.N. 498.

his inn provided he has sufficient room and the traveller is willing to pay usual charges and is not otherwise objectionable. Under the Common Law of England, his liability for loss of or damage to customers' goods is absolute; exceptions being only in case of an act of God, the King's Enemies and the customers' own negligence. This special liability however is not enforced in India, where there is no corresponding institution like the "Inn" of England. It has been held (q), therefore, that the liability of a hotel keeper in India for the goods of his guests is governed by secs. 151-52 of the Contract Act and not by the rules of English Common Law. Notice that the liability for taking care which is enforced by secs. 151-52 on a bailee, cannot be waived by special contract, except in those cases where law allows it (r).

BURDEN OF PROOF: Generally the burden of proving absence of negligence lies on the bailee in the first instance, the loss being itself evidence of negligence. In cases where goods are destroyed by fire through unknown cause during the course of a railway transit, the rule laid down by the Privy Council is that it is for the railway administration, in the first instance, to call all evidence in their possession to show how and with what care the goods were dealt with by them. The plaintiff must then show some act or omission amounting to negligence on their part (s).

Other duties of bailee (secs. 153-63)

The bailee has other duties as well, over and above the duty to take care of the goods bailed. These are: (i) the bailee must not do any act with regard to the goods bailed which is inconsistent with the terms of the bailment. If he does, the bailment is voidable at the option of the bailor (sec. 153). Thus if a horse is taken for riding, it should not be used for driving a carriage.

(ii) If the bailee does any act with regard to the goods bailed which is not in accordance with the terms of the bailment and loss results, the bailee is liable to make good the loss to the bailor (sec. 154). Thus if while driving the horse in the above case, the horse falls and suffers an injury, the bailee is liable in damages therefor, though he may have used due care and caution. The sec. creates a liability independently of contract, so that even a minor can be liable under the sec. (t).

(iii) The bailee must not mix the goods bailed with other goods of his own, without the bailor's consent. If he mixes the goods bailed with his own goods, with the bailor's consent, each has, in the mixture, an interest proportionate to their respective shares (sec. 155). If no consent of the bailor has been taken and goods can be separated, the property in the goods remains with the parties respectively, but the bailee must bear the expense of separation (sec. 156). If, in the above conditions, a separation cannot be effected, the bailor is entitled to recover from the bailee compensation for total loss of the goods (sec. 157).

(iv) The bailee is bound, without demand by bailor, to return the goods bailed to the bailor, or according to his directions, as soon as the time or purpose of the bailment has come to an end (sec. 160). If the bailee fails to do so, he is responsible for any loss, deterioration or destruction of the goods (sec. 161).

(q) Rampal Sing v. Murrey & Co., 22 All. 164.

(r) Sheikh Mahomed v. B.I.S.N. Co., 32 Mad. 95.

(s) Dwarkanath v. Rivers Steam N. Co., 27 C.L.J. 157.

(t) Burnard v. Haggis (1863), 14 C.B.N.S. 45.

(v) Notice, that a gratuitous bailment can be recalled by the bailor at any time, even though it is made for a fixed time or for a particular purpose. But if on faith of the contract, the bailee has acted in such a way that the loss caused by the termination of the bailment, exceeds the benefit derived by the bailee therefrom, the bailor is bound to make good that loss to the bailee (sec. 159).

(vi) In absence of a contract to the contrary, the bailee is bound to deliver to the bailor or according to his directions, any increase or profit from the goods bailed (sec. 163). Thus if shares are deposited by way of pledge, and a bonus is declared, the bonus shares must be delivered back to the bailor along with the original shares.

Gratuitous bailment

This is a bailment without any stipulation for reward: (i) Such a bailment can be terminated at any time, even though originally made for a fixed time or for a special purpose, subject to the conditions laid down by sec. 159 (see above). (ii) Such a bailment is terminated by the death of the bailor or the bailee (sec. 162). (iii) If the bailment involves keeping or carrying of the goods, or doing some work upon them, and there is no stipulation for reward, the bailee is still entitled to recover from the bailor, the necessary expenses incurred by him for the purpose of the bailment (sec. 158). Notice, however, that such a bailee has no right of sale. Thus where furniture was stocked with friends, and the latter, being in want of space, sold it off by auction, after three years, because the whereabouts of the bailor could not be found though notice was given to him, *held*, they were guilty of conversion (*u*).

Rights of Bailee

The rights of a bailee are: (i) The bailor is bound to make good to the bailee the loss which the latter may sustain, by reason of the fact that the bailor had no right to make the bailment or receive back the goods or give directions respecting them (sec. 164).

(ii) If several joint owners of the goods bail them, the bailee is entitled to deliver them back to or according to the directions of any one of them, in absence of a contract to the contrary (sec. 165).

(iii) A bailee is not responsible to the true owner if, he, in good faith, delivers the goods back to or according to the directions of the bailor, if it turns out that he has no title (sec. 166). This is because in law, a bailee is estopped from disputing the title of the bailor (see Evidence Act, sec. 177). Thus where N entrusted certain bales of cotton to L, a warehouse man (*muccadam*), and L thereafter made a pledge of these bales with B for his own purposes, it was held, in a suit by N against L and B, that a *bona fide* return of the goods bailed by B to L, on redemption, was a complete defence to N's suit (*v*). If a person other than the bailor claims the goods bailed, he should apply to the Court to stop delivery of the goods and decide the title thereto (sec. 167). The bailor himself can, in such a case, file an interpleader suit.

(u) *Sachs v. Miklas* (1948), 2 K.B. 23.

(v) *Bank of Bombay v. Nandalal Thaker-*
sidas, 37 Bom. 122.

(iv) The bailee also has (a) a particular lien as well as, (b) in some cases, a general lien on the goods bailed (secs. 170-71, see below).

(v) If a third person wrongfully causes injury to the goods bailed or deprives the bailee of the possession of them, the bailee is entitled to file a suit against the wrong-doer, just as much as the bailor himself is (sec. 180). Anything recovered in such suit shall be divided between the bailor and bailee according to their respective interests (sec. 181).

Rights of a finder (secs. 168-69): A finder of goods being by law (see sec. 71), in the same position as a bailee, his rights are defined by the above secs. These rights are: (i) he has no right to sue the owner for trouble and expense voluntarily incurred by him for preserving the goods and for finding out the true owner, but (ii) he has a right to retain them, i.e. he has a *lien* on the goods for such disbursements, which he may exercise against the true owner. (iii) Where a reward has been advertised, he can sue the owner for the reward if he has found the goods after knowledge of the offer (sec. 168). (iv) Where a thing which is commonly the subject of sale is lost, its finder may sell it, if the owner cannot be found, or if, when found, he refuses to pay the finder his lawful charges, (a) when the thing is in danger of perishing or losing a greater part of its value or (b) where a lawful charges of the finder, exceed two-thirds of its value (sec. 169).

Bailee's particular lien (sec. 170)

Under sec. 170, where the bailee has, in accordance with the purpose of the bailment, rendered any service, involving labour or skill, in respect of the goods bailed, he has a right to retain the goods, till he is paid due remuneration for his services, unless there is a contract to the contrary. This is called the bailee's "*particular lien*". Thus if a diamond has been given to a diamond cutter to be cut and polished he is entitled to a particular lien on the diamond, i.e. he is entitled to withhold delivery of the diamond, till the stipulated amount of his remuneration is paid to him by the bailor.

Three points must be noted with regard to the particular lien of a bailee: (i) it is a possessory lien, i.e. it exists so long only as the bailee has got possession of the thing bailed. If he parts with possession thereof, the lien will disappear. (ii) It exists only in respect of work involving labour or skill. Thus if a motor car is sent to a firm of repairers, the latter have a right to detain the car till the amount due to them for repairs is paid (w). If the services are nominal, or do not improve or enhance the value of the article, no lien can be claimed. Thus in an English case (x), the owner of a motor car, agreed with a company that the latter should maintain and garage the car for three years on payment of an annual sum to them by the owner. On payment being in arrears, the company stopped the owner from taking away the car. *Held*, the company had no lien on the car. (iii) It arises only where there is no contract to the contrary. Thus if a tailor has agreed to give three months' credit to the customer, for payment of his charges for preparing a coat for the customer, he has no particular lien on the coat as against the customer for payment of the charges (see ill.). Similarly, if the bailee takes a security from the bailor for payment of his dues in such a manner as to show that it was intended to be in substitution of the lien, the lien will be gone.

(w) *Green v. All Motors Ltd.* (1917), 1 K.B. 625.

(x) *Hatton v. Car Maintenance Co.* (1915), 1 Ch. 621.

Bailee's general lien (sec. 171)

Under sec. 171, five special types of bailees, viz. (i) bankers, (ii) factors, (iii) wharfingers, (iv) attorneys of a High Court, and (v) policy brokers, are, in absence of a contract to the contrary, entitled to retain, as security for a general balance of account, any goods (belonging to the bailor) which are bailed with them. No other person has such a right, unless there is an express contract to that effect.

The sec. deals with what is called a "*general lien*" as distinguished from the "*particular lien*" described by sec. 170. Both liens are possessory liens. The difference between the two, however, is as follows: (i) a "*particular lien*" attaches only to the particular property, in respect of which charges are due to the bailee; a "*general lien*" attaches to all property of the bailor with the bailee by way of bailment, for amounts due to the bailee for work done with regard to any one or more of them or as the sec. puts it, "for a general balance of account". (ii) A "*particular lien*" is available to all bailees who satisfy the conditions of sec. 170. A "*general lien*" is available to only five types of bailees and to no other, unless by a special agreement. Thus, if A maintains an overdraft account with a bank and also a current account, and he has overdrawn against the first account, the banker would be entitled, under the "*general lien*", given to him by sec. 171, to refuse to allow the customers to operate on his current account till the amount overdrawn against the first account is made good by the customer.

The banker's "*general lien*" extends to all securities of the customer in the possession of the banker by way of bailment, e.g. bills of exchange, cheques, moneys deposited or paid to him as banker and securities deposited with him as such. It also extends to other moneys of the customer held by him as such (x1). It does not extend, however, to securities and other property of the customer deposited with the banker for safe custody or for a special purpose (y). It may also be excluded by a special agreement which may be express or implied. Thus, if securities are deposited to secure an overdraft for a particular amount, this impliedly excludes a general lien for more than the specified sum (z). Notice that a banker is not affected by any defect in title of the customer to the securities in question, provided he has acted in good faith and without notice of the defect.

A "*factor*" is an agent for sale or purchase or both, to whom possession of the property is given by the principal for such purpose. He, generally, purchases or sells in his own name, though on behalf of the principal. He has a general lien on the goods of his principal consigned to him as such factor for all advances made by him against them, for his expenses and disbursements and for all remuneration due to him in respect of them. Of course, no lien can be claimed by him for debts due to him prior to his acting as such factor for his principal. The lien does not attach to goods consigned to him, for a special purpose, e.g. to sell and pay the amount of a specified bill of exchange thereout.

Wharfingers also have a general lien on the goods unloaded and warehoused by them for particular parties. The lien is generally against the consignors.

(x1) *Panjab National Bank v. Satyapal*, A.I.R. (1956) Panj. 118.

(y) *Cuthbert v. Roberts Lubbock & Co.* (1909), 2 Ch. 266.

(z) *Re Bowes* (1866), 33 Ch.D. 586.

Attorneys have a general lien "for all taxable costs, charges and expenses" incurred by them as solicitors for their clients. They have no lien for loans or advances made by them to their clients. The lien extends to all deeds, papers and documents of the client lying with them as such solicitors. The lien may be lost by taking a security in substitution of it. If a solicitor discharges himself, the lien will be lost, but not if the client discharges him.

Policy brokers are also given a general lien. This lien is exercisable by brokers who effect marine insurance policies. In English insurance practice, a policy broker occupies a recognised position. It is he who receives the premium from the assured to be paid over to the underwriter and it is to him that the underwriter hands over the policy to be delivered to the assured. Such brokers have, under the sec., a general lien on the policies in their possession, not only for any premium which may be due by the assured, but also for any other charges that may be due to them from the assured. The brokers' lien, however, may be limited by express agreement (a). This system of brokers, however, is not very common in India.

Liens generally

Lien is a right which the law gives to certain persons in specified circumstances to refuse to deliver property belonging to others, till those others have discharged their legal obligations to them. Liens are of three kinds : (i) possessory lien, (ii) equitable lien, and (iii) maritime lien.

Possessory lien is one which enures only so long as the person claiming the lien has got possession of the property over which it is claimed. In order that such a lien may exist, the possession must be (a) rightful, (b) continuous, and (c) not for any special purpose. Possessory lien only entitles the party to retain possession of the subject-matter of the lien till his claim is satisfied. It gives him no right of sale. No claim can also be made by such person, for storage or warehouse charges with regard to the goods. A possessory lien may be either (i) particular or (ii) general. A particular lien is given by law to (1) bailees (sec. 170), (2) to a finder of goods (sec. 168), (3) to agents (sec. 221), (4) to pledgees (secs. 173-4), (5) to Carriers, (6) to innkeepers, (7) to Railways (under the Railways Act), (8) to ship-owners under the Merchant Shipping Act, (9) to Dock Companies and Port Trust authorities, and (10) to an unpaid vendor under the Sale of Goods Act. The lien is lost by (i) loss of possession of goods ; (ii) by payment or tender of the amount claimed ; (iii) by taking security by way of substitution ; and (iv) by abandonment. A general lien is given by law to the five types of bailees mentioned by sec. 171.

Equitable lien is a lien which creates a charge on the property to which it attaches so that whoever takes it thereafter with notice thereof, takes it subject to the lien. It is created by statute and is in no way dependent on the possession of the property to which it is attached. Thus an unpaid vendor of immoveable property, a purchaser of such property who has pre-paid the price, have an equitable lien on the property for the amounts due to them. A partner who on dissolution of a partnership pays the debts of the partnership has an equitable lien on the assets of the partnership for all sums paid by him on behalf of the partnership. This lien is enforceable by sale.

Maritime lien is a lien which is binding on a ship, and all her furniture, tackle, cargo and freight, for payment of a claim founded on maritime law. It is given by law to (i) the master, for wages and disbursements; (ii) to a bottomry bond-holder, for the amount of the bond; (iii) to salvors, on the property saved; and (iv) to persons having a claim against the ship for damages caused by collision due to the ship's negligence. It is enforced by an action "*in rem*", i.e. against the ship itself, e.g. by arresting the ship, by proceedings in Admiralty Court. The lien subsists notwithstanding a transfer of the ship, even to a *bona fide* purchaser for value (b).

Pledge (sec. 172)

A pledge is defined by the sec. as "a bailment of goods as security for the payment of a debt or the performance of a promise". The bailor is called the "pawnor" or "pledgor" and the bailee is called the "pawnee" or the "pledgee". Thus if A being in need of money, raises money from a money-lender, on the security of his watch and chain, the transaction is one of pledge. Notice that before a pledge can be valid, the bailor must be in "juridical possession" of the goods, i.e. in possession of the goods under a legal right or title. Thus a servant cannot make a valid pledge of his master's goods, though he may have "possession", i.e. the physical custody of them.

Pledge distinguished from Bailment and Mortgage

A pledge is thus distinguishable from an *ordinary bailment*: (i) in a pledge, the bailment is made as security for the due discharge of a legal obligation. In ordinary bailment, there is no such idea. (ii) On a bailment of goods, what passes to the bailee is a right of possession of the goods bailed; on a pledge, the pledgee obtains "a special property" in the goods pledged (c). (iii) A bailee has a right of lien on the goods bailed, but no right of sale. A pledgee has such a right, under certain circumstances (see seq.). The above points also distinguish a pledge from a lien.

A pledge must also be distinguished from a *mortgage of moveables*. There is no specific statutory provision either in the Contract Act or in the Transfer of Property Act, for a mortgage of moveables (otherwise known as hypothecation). Such transactions however are not on that account invalid (d). A mortgage of moveables is distinguished from a pledge as follows: (i) a mortgage of moveables transfers to the mortgagee, the ownership of the property, with only a right of redemption left in the mortgagor. A pledge transfers to the pledgee only a right of possession and a qualified right of sale. (ii) A pledge requires delivery of possession in order to be valid, a mortgage of moveables does not require delivery of possession as an essential pre-requisite. (iii) A mortgagee of moveables has the rights of foreclosure and sale, the pledgee has only a limited right of sale (e). Notice that a mortgage of moveables does not require either writing or registration to be effective in law but can be made orally (f). In the last mentioned case, Beaman J. pointed out the difficulties which this anomaly gives rise to. Though such a mortgage is valid without transfer of posses-

(b) *The Bold Buccleugh*, 7 M.I.A. 267.

(c) *Ex parte Hubbard* (1886), 17 Q.B.D. 698.

(d) *Damodar v. Atmaram*, 8 Bom. L.R. 344.

(e) *Halliday v. Holgate* (1868), L.R. 3. Ex. Cases 299.

(f) *Tahilram v. D'Mello*, 18 Bom. L.R. 587.

sion, a subsequent dishonest pledge of the same property by the mortgagor, would give the pledgee a priority over the mortgagee, if the pledgee has acted in good faith and without notice of the prior mortgage.

Rights of pledgee (secs. 173, 174 and 177)

A pawnee has the following rights: (i) Under sec. 173 a "right of retainer" against the goods pledged, for payment of the debt (for which pledge is created) with interest thereon, as also for all necessary expenses incurred by him in respect of the possession or for the preservation of the goods. He has no such right of retainer against the goods, in respect of any other debt or liability owing by the pledgee to him, unless there is a contract to that effect. However, such a contract shall be presumed to exist with regard to any subsequent advance made by the pledgee to the pledgor (sec. 174).

(ii) He is entitled to recover from the pledgor all extraordinary expenses incurred by him for the preservation of the goods (sec. 175). He has no "right of retainer", however, for such expenses.

(iii) The pledgee has also a limited right of sale under sec. 176. Under the sec., if the pawnor makes default in payment of the debt or performance of the promise, the pawnee may (a) bring a suit against the pawnor upon the debt or promise and retain the goods pledged as collateral security or (b) he may sell the thing pledged after giving the pawnor a reasonable notice of the sale. In such a case, if the proceeds of the sale are insufficient, the pawnor remains liable for the deficit, if they are in excess, the pawnee must pay over the surplus to the pawnor. (c) A third right which the pawnee also has is a right to file a suit to have the pledged property sold through Court (g). Notice that a pawnee may sell the goods pledged by public auction or by private treaty. He cannot, however, buy the goods himself at such a sale. Such a purchase would be void (h). Notice further that, as has been held by the Bombay High Court in a recent case (i), notice to the pawnor of the proposed sale is essential even though the instrument of pledge contains an unconditional power of sale. Where no such notice is given, the sale of the pledged goods by the pledgee is void and does not destroy the pledgor's right of redemption. The fact that the purchaser at such sale purchased the goods *bona fide*, and without notice that the pledgee had no right to sell, does not protect the purchaser. The pledgor, therefore, is entitled to redeem the goods, pledged, even in the hands of such purchaser. This is because of sec. 177, which provides that the defaulting pawnor is, in law, entitled to redeem the pledge, any time before the actual sale thereof by the pledgee. The Court in the above case held that by the word "sale" in the above sec. is meant a "lawful sale" and not an invalid sale. On such redemption, the pawnor is bound to make good to the pawnee all expenses which have resulted from his default (sec. 177). A pledgee bank whose right to deal with the securities pledged would arise only on the happening of certain events, e.g. that the pledgor either fails to maintain the proper margin or makes default in payment of outstanding amount on demand, has been held to have no right to deal with the securities, either

(g) Off. Assignee v. Sarju (1945), All. 373.

(h) Neckram v. Bank of Bengal, 19 I.A.

(i) Off. Assignee v. Madholal, 48 Bom. L.R. 828.

by way of pledge, sub-pledge or assignment, so long as these events have not happened. If it does so, it would be liable in damages (i).

Pledge, how far valid (secs. 178, 178A, 179)

Generally speaking, on a pledge of goods, what passes to the pledgee is the interest which the pledgor has in the subject-matter of the pledge. As sec. 179 provides, if such a pledgor has a limited interest in the thing pledged, the pledge is valid only to the extent of that interest. In certain cases, however, a pledge may be valid as such, though the pledgor's title to the thing pledged is defective. These cases are provided for by secs. 178 and 178A :

(I) Under sec. 178, where (i) a mercantile agent, is (ii) with the consent of the owner, (iii) in possession of goods or documents of title to goods, any pledge made by him, (iv) while acting in the ordinary course of business as mercantile agent, shall be as valid as if the true owner had expressly authorised the same, provided (v) the pawnee acts in good faith and (vi) without notice that the pawnor had no authority to pledge. All the six conditions mentioned above must be fulfilled before the exception can operate. Thus an ordinary agent or a person in bare custody of the goods, e.g. a wife or a servant, cannot make a valid pledge under the sec. A person entrusted with the possession of goods of another for a special purpose is also not covered by the sec. (j). He must be a "mercantile agent" as defined by the Sale of Goods Act. Is a broker to whom goods are entrusted for sale on "jangad" terms, within the sec. ? If the terms of agency include a power of sale to an approved customer, the case would apparently be within the sec. (k). It would be otherwise, if the authority was merely to show the goods to prospective customers. The person must be in possession of the goods, with the consent of the true owner. Thus goods obtained by theft cannot be the subject of a valid pledge under the sec. What can be pledged under the sec. are both goods and documents of title to goods as defined by the Sale of Goods Act. The person must pledge the goods in the ordinary course of his business as mercantile agent. Thus where share certificates with the relevant transfer forms are given to a certified share-broker for the purpose of effecting a sale thereof, a fraudulent disposal of the same by the share-broker in question by way of pledge, would be valid and binding on the true owner under the sec., if the other conditions of the sec. are satisfied (l). This is because "shares" are "goods" under the Sale of Goods Act. Of course, the pawnee must act in good faith and without notice that the pledgor's title is defective.

(II) The second exception is under sec. 178A, under which where the pawnor has obtained possession of the goods under a contract voidable under secs. 19 and 19A of the Contract Act (i.e. on the ground of coercion, fraud, misrepresentation and undue influence), but the contract is not rescinded at the time of the pledge, the pawnee acquires a good title to the goods, provided he acts in good faith and without notice of the pawnor's defect of title. The sec. protects a pledge by a person in possession of goods under a *de facto* contract, which contract however is voidable for various reasons. It does

(i) *Jaswantrai Akhanay v. State of Bombay*, A.I.R. (1956) S.C. 575.

(j) *Ramasami v. Kamalammal*, 45 Mad. 173.

(k) *Durgabai v. Saraswatibai*, 31 Bom. L.R. 414.

(l) *Fazal v. Mangaldas*, 48 Bom. 489.

not protect a pledge by a person in possession of goods, where there is no contract between him and the true owner, e.g. a pledge of goods by one who has obtained them by means of theft.

Two more exceptions may be added to the above, under sec. 30 of the Sale of Goods Act, viz. (III) a pledge by a person in possession of the goods, or of documents of title to goods, after sale of the goods by him to a third person, confers good title to the pledgee, provided the latter has acted in good faith and without notice.

(IV) Similarly, a pledge by a person in possession of goods or of documents of title to goods, with the consent of the unpaid seller, under a purchase or an agreement of purchase by him, will be binding on the seller, if the pledgee has acted in good faith and without notice of the defect of the pledgor's title (see sec. 30, Sale of Goods Act seq.).

CHAPTER IX

AGENCY

Agent defined (sec. 182): An agent is defined by the sec. as a "person employed to do any act for another or to represent another in dealings with third persons". The essential characteristics of an agent are: (i) that his acts, if within his authority, are binding on the principal and (ii) that he himself is not generally liable for what he does on behalf of his principal. He is merely what is called a "conduit pipe".

Different kinds of agents

Various kinds of agents are known in trade and commerce. A **broker** is an ordinary agent, who, for reward, agrees to bring about a transaction on behalf of his principal, or to carry out any other instruction given by his principal. He generally acts on behalf of and in the name of the principal. His reward or "commission" is ordinarily not due till the transaction for which he is employed is actually put through.

A **factor** is an agent who is entrusted with the possession of goods by his principal with authority to sell the same. He is entitled, in law, to sell the goods of his principal in his own name. Frequently, he advances moneys to his principal on the security of the goods, the agreement being that the factor should reimburse himself for his advances from the sale proceeds of the goods. In such a case, his agency is called "an agency coupled with interest" (see seq.) which the principal cannot terminate by mere notice. A factor has a general lien on the goods of his principal in his possession for a general balance of account. Under the terminology used by the Sale of Goods Act, such an agent will be a "mercantile agent".

An **auctioneer** is an agent both for the seller as well as the purchaser. He advertises and conducts the sale as agent of the seller. On the final fall of the hammer, he becomes the agent of the highest bidder, i.e. the buyer. He can recover the price from such purchaser by filing a suit in his own name. He has a particular and not a general lien on the goods in his

possession. He, however, does not warrant his principal's title to the goods, which are offered for sale (m).

A **commission agent** is an agent who buys or sells in the market on behalf of his principal, as per his instructions. He is not liable for the failure of the other party to the agreement to carry out his part thereof. He cannot charge a higher price to his principal than that which is charged to or by him.

An **indentor** is a commission agent, who for a pecuniary reward puts through a transaction of sale or purchase on behalf of his principal, with a merchant in a foreign country. According to a custom judicially recognised in Bombay, an indenting firm is entitled to charge to their principal in Bombay, the rates mentioned in the indent (n).

Estate brokers are agents who find purchasers or sellers of property on behalf of their employers. Generally they are entitled to their commission when they bring about a contract between their employer and a party who is both willing and able to purchase or sell (o). If thereafter the contract goes off by reason of his employer's default, the broker would be entitled to his commission, unless the contract provides for payment of commission only after the transaction is completed (p).

A **del credere agent** is an agent who not only establishes a privity of contract between his principal and the third party, but who also guarantees to his principal the due performance of the contract by the third party. He is liable, however, only when the third party fails to carry out his contract, e.g. by insolvency. He is not liable to his principal if the third party refuses to carry out his contract, e.g. if the buyer refuses to take delivery (q). Certified share and stock brokers of the Bombay Native Stock and Share Brokers' Association are *del credere agents* of their constituents (r).

An agent may be a **general agent** or a **particular agent**. He is the latter when he is employed by his principal for doing a particular act, e.g. to buy a particular property. He is the former, when he is employed by his principal to represent him in a series of transactions of a particular kind, e.g. a gumasta who conducts his principal's business on the latter's behalf.

A **sub-agent** is an agent properly employed by the agent and acting under the instructions and authority of the agent (sec. 190). A **substituted agent** is an agent appointed by the agent, but acting under the control of and under the instructions of the principal (sec. 194).

Pakka and Katcha Adatias: These are two special types of agents who have obtained legal recognition by reason of their constant use by the mercantile community of this country. A **pakka adatia** is an agent who guarantees the performance of the contract, not only to his own principal but also to the broker (called "shroff") on the other side. He has this further peculiarity also, viz. that in carrying out his principal's instructions (to buy or to sell), he can substitute his own contract instead of a contract with a third party. Thus he is an agent, upto a certain stage, e.g. in carrying out his principal's instructions but beyond that stage, he is a principal also, as

(m) *Benton v. Campbell Parker & Co.* (1925), 2 K.B. 410.

(n) *Paul Bier v. Chhotalal*, 30 Bom. 1.

(o) *Poole v. Clarke & Co.* (1945), 2 A.E.R. 445.

(p) *Luxor v. Cooper* (1941), A.C. 108.

(q) *Gabriel & Sons v. Churchill & Sim* (1914), 3 K.B. 1272.

(r) *Fazal v. Mangaldas*, 46 Bom. 489.

by custom, he is permitted to deal on his own account in the business of agency (s). A katcha adatia, on the other hand, is an agent merely (t).

Agent and Independent Contractor: An agent has to be distinguished on the one hand, from a servant, and on the other hand, from an independent contractor. A servant acts under the direct control and supervision of the master and is bound to conform to all reasonable orders given to him in the course of the work. An independent contractor on the other hand is entirely independent of any control or interference from his employer and merely undertakes to produce a certain result, employing his own means to produce it. An agent though bound to exercise his authority in accordance with all lawful instructions given to him by his principal is not, in its exercise, subject to the direct control or supervision of the principal. An agent as such is not a servant but a servant is generally for some purposes his master's implied agent, the extent of the agency depending upon the duties or position of the servant (u).

Who may be appointed and who may appoint agent (secs. 183-4): Any person who is of a sound mind and has reached the age of majority according to the law to which he is subject may appoint an agent (sec. 183). As between the employer and third parties, any person may be an agent (e.g. even a minor), but no person who is not of the age of majority and of sound mind, can become an agent, so as to be responsible to his principal as such agent (sec. 184).

How agency can be created

A person may be appointed agent either (i) by express agreement, or (ii) by implication, or (iii) by necessity. (iv) A person may also be held liable as agent, by holding out.

Express agency: A person may be appointed agent, either by word of mouth or by writing. No particular form is required for appointing an agent. Sometimes, however, a person is appointed by another, to represent him in a particular transaction or to sign a particular document on his behalf. In such a case, a formal deed of appointment is drawn up and signed by the principal, which is called a "*power of attorney*". A power of attorney may be (i) general or (ii) special. When it empowers the agent to represent the principal for all purposes generally, it is called a "general power of attorney". When it authorises the agent to do a particular act or acts on behalf of the principal, it is called a "special power of attorney".

Implied Agency arises when, there being no express appointment of a person as agent, the principal conducts himself towards the other and the outside world, as if he were his agent, e.g. regularly sending goods to a commission agent for sale and accepting the transactions effected by him over a long period; an upcountry party repeatedly ordering out articles from another, resident in the city and paying for them. Notice in this connection that where husband and wife are residing together, the wife is impliedly presumed to be the husband's agent to pledge his credit for necessities suited to their condition in life. The presumption, however, is rebuttable, e.g. if the husband has expressly forbidden the wife to pledge his credit or where he has provided sufficient allowance to the wife.

(s) *Bhagwandas v. Kanji*, 30 Bom. 50.

(t) *Fakirchand v. Doolubh*, 7 Bom. L.R.

(u) *Laxminarayan, etc. & Son Ltd. v. Govt. of Hyderabad*, A.I.R. (1954) S.C. 364.

Agency of necessity arises where there being no express or implied appointment of a person as agent for another, the law, by a rule, postulates agency between them, because the necessities of the case make it imperative to do so. Thus a Master of a ship is an agent of necessity of the ship-owner to raise money on the security of the ship or cargo in order to prosecute the voyage when the ship is in distress or is in need of heavy and urgent repairs. Similarly, if a husband improperly leaves his wife without providing proper means for her sustenance, the wife is regarded in law as the agent of necessity of the husband to pledge his credit to secure such sustenance. This rule does not apply where the wife improperly leaves the husband. For "agency by holding out" see seq. Notice that no consideration is necessary to create an agency (sec. 185).

Agent's authority (secs. 186-89)

The authority of an agent may be either (i) express or (ii) implied (sec. 186). It is "express" when it is given by words spoken or written. It is "implied" when it is to be inferred from the circumstances of the case. In this connection, things spoken or written, or the ordinary course of dealing, may be regarded as circumstances of the case (sec. 189). Thus where A leaves his shop in the possession and management of his munim B and A is in the habit of accepting and paying for all transactions affected by B in A's name, B will be deemed to have implied authority from A to enter into transactions on behalf of A in A's name.

Sec. 186 defines the *extent of an agent's authority*. Two rules are laid down. Under the sec. (i) where an agent has authority to do an act, he has also (by law) authority to do every lawful thing which is necessary to do such act; (ii) an agent having authority to carry on a business, has authority (a) to do every lawful thing necessary for the purpose or (b) which is usually done in the course of conducting such business.

The sec. contemplates and provides for two kinds of agents: (i) a special agent and (ii) a general agent (see ante). As regards the first, the provision is that if an agent is appointed to do a specific act, e.g. to enter into a particular contract, this authority would include in itself, authority to do all necessary and lawful things to achieve the purpose, e.g. if the contract can be entered into through the employment of a particular kind of broker (e.g. a certified share-broker), to employ such broker, for his principal. If an agent is appointed to sell property, he has implied authority to describe the property and state circumstances which may affect its value. As regards a general agent, e.g. an agent to conduct a business, the sec. makes the extent of his authority dependent upon, not only what he has been expressly authorised, but also on what is *necessary for or usually* done in carrying on such business. It becomes a question of fact in each case, therefore, whether what is done by an agent, is such as conforms to the standard set up by the sec.

The question has been settled by decisions, however, in some cases. Thus the authority of an agent to carry on a mercantile business, does not imply an authority to draw, endorse or accept bills of exchange in the name of the firm (v). An agent to carry on a money-lending business, however, has been held entitled to borrow money on behalf of the firm and to pledge

the principal's credit to secure such advances (*w*). A factor has authority to sell goods in his own name and to receive payment thereof in his own name. He is entitled to give reasonable credit. He has also authority to warrant the goods sold, if such warranty is usual in the trade (*x*). He however cannot delegate his authority to another.

A **broker** has authority to act under and according to the rules and regulations of the market in which he deals, unless such rules are unreasonable or unlawful (*y*). If he is authorised to sell, he can give reasonable credit. He cannot however cancel or vary a contract which he has once entered into on behalf of his principal. He cannot receive the price of goods sold, when the principal is disclosed; otherwise, where he is acting for an undisclosed principal (*z*). He cannot delegate also.

An **auctioneer** has implied authority to contract on behalf of the seller as well as the buyer as regards goods sold by auction. He has no implied authority to effect a private sale. He has no authority to take a bill of exchange in lieu of the price. If there is a custom to that effect, he can accept a cheque. He has no authority to warrant the goods sold or to give delivery thereof, except as against the payment of the price.

A **pleader** has no authority to settle his client's case except under his specific instructions. A **counsel**, however, has such authority, by virtue of his special retainer. He has no authority to settle, however, where the client has expressly prohibited him from so doing.

An **attorney** is entitled to settle his client's case, if he does so, *bona fide*, with sufficient skill and if the settlement is reasonable. For a Master's authority see seq.

(iii) The last rule with regard to an agent's authority is laid down by sec. 189. Under the sec., an agent in an **emergency**, is entitled to do all such acts for the purpose of protecting his principal from loss as a prudent man would do in his own case, under similar circumstances. Thus if goods are consigned by A to B for sale at C and when they reach B they are in danger of being spoiled by further journey to C, B has authority to sell them off immediately, at his own place, without despatching them to C (see ill.).

Notice that an agent can in no case have authority, either express or implied, to do that which his principal himself, e.g. an incorporated company, could not do (*a*).

Sub-Agent (secs. 190-95)

The general rule of law is "*delegatus non potest delegare*", which means that where authority is delegated (coupled with discretion or confidence), it cannot be further delegated. This principal is recognised by sec. 190 which provides that an agent cannot lawfully employ another to perform acts which he has expressly or impliedly undertaken to perform himself, *unless* (i) by the ordinary custom of trade a sub-agent may or (ii) from the nature of the agency a sub-agent must be appointed. A sub-agent may therefore be lawfully employed by an agent, (i) when expressly autho-

(*w*) Bank of Bengal v. Ramanathan, 43 A.A. 44.

(*x*) Dingle v. Hare (1859), 7 C.B.N.S. 145.

(*y*) Cropper v. Cook (1868), L.R. 3 C.P.

194.

(*z*) Campbell v. Hassel (1816), Stark 233.

(*a*) Sutlej Cotton Mills v. Dr. Ranjit Sing, A.I.R. (1952) Cal. 263.

rised by his principal, (ii) if it is usual in the business of agency to employ him, and (iii) where the nature of the case requires such employment.

In this connection notice that factors, brokers, auctioneers, directors and liquidators have been held not to be entitled to delegate their authority to sub-agents. On the other hand, architects and builders have been held entitled to employ surveyors to have the quantities worked out from their reports. Notice further that if the act is purely ministerial, it can always be delegated (b). The nature of the agency may also require such employment, e.g. where an agent is appointed to recover moneys by filing a suit, the agent would be entitled to appoint an attorney for the legal part of the work.

Sub-Agent defined (sec. 191): A sub-agent is a person (i) employed by and (ii) acting under the control of the agent. Such a "sub-agent" must be distinguished from what is known as "*substituted agent*". The latter is defined by sec. 194, according to which, where an agent holding an express or implied authority to name another person to act for his principal, names another person accordingly, he is not a "sub-agent" but a "*substituted agent*" for the principal. In other words, both in the case of a "sub-agent" as well as a "*substituted agent*", the appointment is by the agent but whereas in the case of a "sub-agent", he acts under the control of and under the directions of the agent; in case of a "*substituted agent*", he is an agent of the principal and is, therefore, bound to act under his control and according to his directions (c). Thus if A appoints B, a solicitor, to sell his estate by auction and to employ an auctioneer for the purpose, the auctioneer so employed, is not a "sub-agent" of B but is a "*substituted agent*" of A (see ill.).

Under sec. 195, the agent when authorised by his principal to name another person as such substituted agent, must exercise the same amount of discretion as a man of ordinary prudence would do in his own case and if he does so, he is not responsible for such agent's neglect or default.

Effects of appointment of sub-agent (secs. 192-93)

The above secs. lay down the legal consequences of the appointment of a sub-agent. A sub-agent may be appointed by the agent (i) properly, i.e. in cases in which he is entitled (under sec. 190) to appoint such sub-agent, or (ii) improperly, i.e. without legal justification for such appointment. Both cases are considered separately :

Where a sub-agent is properly appointed, the result, under sec. 192, is as follows : (i) as between the principal and third parties, the principal is bound by the acts of such sub-agent and is also represented by him ; (ii) the agent is responsible to the principal for the acts of the sub-agent ; and (iii) the sub-agent is not responsible to the principal, except in the case of fraud and wilful wrong. Thus if A owes money to B and C has authority to collect money for B, a payment by A to D, who is the servant of C, would be a good payment to B, as D is the sub-agent properly appointed under the sec. In such a case, B cannot call upon D to account for the moneys received, as there is no privity between the two, but B can call upon C to account for D's receipt of the moneys and C can call upon D to do the same

(b) *Ex parte Birmingham Banking Co.* (1868), L.R. 3 Ch. 461.

(c) *De Bussche v. Alt.* (1878), 8 Ch.D. 310.

to him. It would be different if D has committed a fraud, e.g. received a secret commission (d).

Where a sub-agent is improperly appointed, (i) the principal is not represented by or bound by the acts of such sub-agent, as between himself and third parties; (ii) the sub-agent is responsible to the agent, as if the latter were the principal; (iii) the agent is responsible to the principal as well as third parties for the act of the sub-agent; and (iv) the sub-agent is not responsible to the principal at all (sec. 193).

In a Bombay case (e), the plaintiff had consigned 441 bales of cotton to the defendants in Bombay for sale on commission and the defendants advanced against the bales 80 or 85 per cent of the market value of the goods. The railway receipts were handed over by them to a firm of muccadams, who took delivery of the bales and stored them in their godown. The muccadams were employed by the defendants and their charges were first paid by the defendants and then debited by them to plaintiffs' account. The duties of the muccadams were to store, to sell and give delivery of the bales. The muccadams fraudulently disposed of 117 bales, after they were authorised by the defendants to sell them and then became insolvent. Held, the muccadams were the sub-agents of the defendants and as they had committed a fraud in the course of employment which was authorised, the defendants were liable to make good the loss to the plaintiffs.

Ratification (secs. 196-200)

Under sec. 196, where a person does an act for another but without his knowledge or authority, such other person may elect to ratify the act. If he does so, it will have the same effect as if the act was originally done by his authority.

Before the doctrine of ratification can apply to the act of an agent done without or in excess of the principal's authority, the following conditions must be fulfilled: (i) it must be done on behalf and in the name of the principal. If the act was done by the agent in his own name, the principal cannot make it his own by subsequent ratification (f).

(ii) The principal must be competent to contract. Thus an act done on behalf of a minor without authority, cannot be validated by his subsequent ratification after attaining majority.

(iii) The principal must be an existing person. Thus an act done by promoters for a company about to be formed, cannot be made the company's act by the company ratifying the same after formation (g).

(iv) The act must be legal and capable of being ratified by the principal. Thus acts of directors which are *ultra vires* the company, cannot be ratified by subsequent resolution of the company.

(v) The ratification must be with full knowledge of all the material facts, a ratification without such knowledge being bad under sec. 198.

(vi) The whole act must be ratified and not only a part of it (sec. 199).

(vii) An act, which, if done with knowledge, would have the effect of exposing a third party to damages or of terminating the right or interest of such party, cannot, by subsequent ratification, be made to have such effect

(d) Powell v. Jones (1905), 1 K.B. 11.

(e) Nensukh v. Birdichand, 19 Bom. L.R. 948.

(f) Keighley Maxted & Co. v. Durant (1901), A.C. 240.

(g) Kelner v. Baxter (1886), L.R. 2 C.P. 174.

(sec. 200). Thus a notice to quit, unauthorisedly given by an agent, on behalf of his principal, cannot, by subsequent ratification by the latter, be made valid notice to quit, so as to cause the termination of the tenancy (see ill.). In other words, rights of property cannot be changed by subsequent ratification of what initially was an inoperative act.

Termination of agency (secs. 201-10)

An agency may come to an end in a variety of ways: (i) by the principal revoking his authority; (ii) by the agent renouncing the business of agency; (iii) by the business of agency being completed; (iv) by the principal or agent dying; or (v) becoming of unsound mind; and (vi) by the principal being adjudicated insolvent (sec. 201).

As regards (i) above, notice that as sec. 202 lays down, the principal cannot revoke an agency coupled with interest to the prejudice of such interest. Agency is "*coupled with interest*", when the agent has himself an interest in the subject-matter of the agency, e.g. where goods are consigned by an upcountry consignor to a commission agent for sale, with power to recoup himself from the sale proceeds, the advances made by him to the principal against the security of the goods; in such a case the principal cannot revoke the agent's authority till the goods are actually sold, nor is the agency terminated by death or insanity (see ill. to sec.). Notice, however, that the mere fact of the commission agent having made advances to the principal, will not have the effect of making his agency, an agency "*coupled with interest*" (h). Similarly, a rent collector whose salary is agreed to be paid from the collections, is not within the sec. (i).

The principal also cannot revoke the agent's authority after it has been partly exercised, so as to bind the principal (sec. 204), though he can always do so, before such authority has been so exercised (sec. 203). Thus if A authorises B to purchase 100 bales of cotton on his behalf and pay for them out of A's moneys in his hands, A cannot terminate B's agency after B has actually purchased the bales and made himself personally liable to pay the price thereof (see ill.).

Further, as laid down by sec. 205, if the agency is for a fixed period, the principal cannot terminate the agency before the time fixed, except for sufficient cause. If he does, he is liable to compensate the agent for the loss caused to him thereby. The same rules apply where the agent renounces an agency for a fixed period. Notice in this connection that want of skill, continuous disobedience of lawful orders, and rude or insulting behaviour, have been held to be "*sufficient causes*" for the dismissal of an agent. Further, reasonable notice of such revocation (or renunciation) must be given, by one party to the other; otherwise, damage resulting from want of such notice, will have to be paid (sec. 206). What is reasonable notice is a question of fact. The period will vary with the nature of the employment. Thus to an ordinary servant, a month's notice would be reasonable, but when the plaintiffs had acted as the chief insurance agents of a large and flourishing insurance company for a period of over fifty years and had secured to the company, business running into several lakhs a year, it was

(h) Jafferbhay v. Charlesworth, 17 Bom. 520.

(i) Vishnucharya v. Ramchandra, 5 Bom. 253.

held by the Privy Council that a three and a half months' notice of termination of agency was not sufficient (j).

Notice that a revocation or renunciation of an agency may be made expressly or impliedly by conduct (sec. 207). The termination, however, does not take effect, as regards the agent, till it becomes known to him and as regards third parties till it becomes known to them (sec. 208). Thus a sale of the principal's goods by an agent, after the latter's authority is revoked, is bad as between him and his principal, but it will be binding on the latter, if the purchaser purchased, *bona fide*, without notice of the agent's want of authority. Similarly, if A directs his agent B to pay money to C, but dies before such payment and B pays the amount to C in ignorance of A's death, the payment will be good payment as against the estate of A in the hands of A's executors (see ill. to sec.).

Notice further that where an agency is terminated, by the principal dying or becoming insane, the agent is bound to take all reasonable steps for protecting and preserving the interests entrusted to him, for the benefit of his representative (sec. 209). Where an agent's authority is terminated, it operates as a termination of the authority of the sub-agent also (sec. 210). Payment made to an agent after knowing the termination of his authority, does not bind the principal (j1).

Agent's duties towards the Principal (secs. 211-21)

The duties of an agent towards his principal are: (1) to conduct the business of agency according to the *directions of his principal* and in the absence of such directions, according to the custom of the business in the place where it is conducted. If the agent acts otherwise, he is liable for any loss sustained. If any profit accrues, he must account for it to the principal (sec. 211). Thus where A was directed by his principal to warehouse his goods at a particular place but he warehoused a portion of them at another, where they were destroyed by accident, it was held that the agent was liable to make good the loss (k). Where an agent bought a larger quantity of goods than was ordered by the principal, it was held that the principal was entitled to a refund of the purchase price from the agent (l). Where an agent was directed to give delivery against cash and he delivered the goods without payment of the price, he was held liable in damages for the price which the purchaser failed to pay (m). Where a share-broker wrongfully closes his client's transaction, the client can complain only in any one of two forms: either that the broker has made a profit out of the transaction, in which case he is accountable for it or that the shares have not been sold at the market price, in which case he is liable in damages (n). When agents in Bombay specifically instructed to insure goods against fire failed to insure them and the goods were lost by reason of the dock explosion of 1944 or the fire caused thereby, *held*, the agents were liable for the loss caused to the principals by their negligence. As Government by an Ordinance had agreed to make good half the losses caused to uninsured goods

(j) *Medora v. Oriental Government Security etc. Co.*, 48 Bom. L.R. 123.

(j1) *Narayan v. Shankar*, A.I.R. (1955) Nag. 202.

(k) *Lilley v. Doubleday* (1881), 7 Q.B.D. 590.

(l) *Bostock v. Jardine* (1865), 3 H. & C. 700.

(m) *Paul Bier v. Chhotalal*, 30 Bom. 1.

(n) *Maneklal v. Jwaladat Pillani*, 48 Bom. L.R. 727.

the agents were held liable to make good the remaining half to their principals (o).

(II) The agent is bound to conduct the business of agency *with such skill as* is generally possessed by persons in similar business, unless the principal has notice of his want of skill. He must act with reasonable diligence. If loss accrues because of his want of such skill or by his neglect or misconduct, he must make good the same to the principal (sec. 212). Thus if A employs an insurance broker to effect a policy on goods on his behalf, and the broker, through negligence, omits to see that proper clauses are included therein, the broker will be liable to make good the loss which is caused to the principal by reason of the goods not being properly covered (see ill.).

Notice that an agent is not liable for mere error of judgment, if he has in fact exercised proper care and skill (p); the sec. makes no distinction also between a gratuitous and non-gratuitous agent as it exists in English Law.

(III) The agent is bound to *render proper accounts* to the principal on demand (sec. 213). If the agent fails to keep proper account of the principal's business, everything consistent with the proved facts will be presumed against him. If the agent has rendered accounts to the principal and the same have been accepted by the latter, the accounts become "settled" or "stated accounts" and cannot be reopened by the principal, except on the ground of fraud, mistake or some other ground which a court of law regards as unconscionable. As pointed out by the Bombay High Court in a recent case (n), in order to be "settled accounts", it is not necessary that the settlement of accounts should be in writing, nor is it necessary that the parties should sit down, compare accounts, and call for vouchers, etc. It is also not necessary that the party to whom they are rendered should have actually seen the accounts and all the particulars and have satisfied himself with its correctness. All that is necessary is that the party to whom they are rendered, should have accepted them as correct; which acceptance again, may be either express or may be implied by conduct.

Rendering accounts does not mean the showing of the accounts but of the accounts supported by vouchers (q). It has been recently held (r), that where an agent does the business of agency in a foreign country, e.g. putting through transactions on the New York Exchange, memoes or statements of accounts sent from such foreign country are sufficient proof as regards ready transactions. As regards forward transactions, however, the same must be proved by proper evidence that the business was in fact done. Where an agent dies without rendering accounts, his estate in the hands of his legal representatives is liable for whatever may be found due to the principal on the account. The principal can file a suit against such representatives, but the onus in such a case is on the plaintiff; the defendants cannot be called upon to account in the technical forensic sense in which an agent may be called upon to do (s).

(IV) The agent is bound in cases of difficulty, to use reasonable diligence to communicate with the principal and seek his directions (sec. 214).

(o) Panalal v. Mohanlal, 53 Bom. L.R. 472.

(p) Lagunas Nitrate Co. v. Lagunas Nitrate Syndicate (1899), 2 Ch. 392.

(q) Anandprasad v. Dwarkanath, 6 Cal.

574.

(r) Shri Meenakshi Mills v. Ratilal, 43 Bom. L.R. 53.

(s) Parshotam v. Ramkrishna, 46 Bom. L.R. 649.

(V) The agent *cannot deal on his own account* in the business of agency without the consent of the principal and without acquainting the latter with all material facts within his knowledge. If he does so, the principal may repudiate the transaction, if the case shows either that a material fact was dishonestly concealed by the agent or that the dealings were disadvantageous to him (sec. 215). Thus an agent employed to sell, cannot buy himself (t). He must not also act for the other party without the consent of his principal nor must he accept any commission from such party (u). Where A employed B as stock broker to buy some shares for him and B without actually buying any shares, sent a contract note to A showing a purchase from third party and actually sold his own shares to A, it was held that A was entitled to repudiate the transaction (v). Under sec. 216, the principal in such a case, is also entitled to claim from the agent, the benefit which has resulted to him from the transaction. The principal, therefore, can also recover from the agent the secret commission or any other special profit which has resulted to him, by acting on his own account in the business of agency. It is immaterial in such cases, that the agent ran the risk of a loss, in acquiring such profit (w). It has been held that the principal can also recover from the agent and the person who has dishonestly paid him such secret commission or bribe, the loss sustained by him by reason of entering into the contract (x) and the fact that the principal has recovered the bribe from the agent is no bar to such action. An agent making a secret profit for himself is also not entitled to his commission or other remuneration (y). The principal, in such a case, can also dismiss the agent without notice (z). Profits acquired by an agent outside the course of agency, however, are not recoverable (a).

(VI) Subject to his right of retainer (see seq.), the agent is bound to *pay to the principal all sums received on account* (sec. 218). Thus if money is paid to an agent on behalf of the principal, by a person indebted to the latter, the agent is not entitled to appropriate the payment to another debt which the same person may owe to him (b). It makes no difference that the transaction in respect of which the payment was received was void or even illegal (c). Thus an agent receiving moneys in respect of a wagering contract is accountable for the same to his principal (d). It is otherwise, if the agency itself is illegal (e).

The agent may, however, under sec. 217, retain, out of moneys received by him on account of the principal in the business of agency, all sums due to himself (i) in respect of advances made, (ii) expenses incurred by him in conducting the agency business as also (iii) all sums due to him as and by way of remuneration. This is known as the agent's **right of retainer**. It extends under the sec. to three items only: (i) expenses, (ii) disbursements, and (iii) remuneration. Notice that no question of limitation can arise, when the agent exercises this right as regards the principal's moneys in his hands.

(t) *Charter v. Trevelyan* (1844), 11 Cl. & F. 732.

(u) *Grant v. Gold Exploration Syn.* (1900), Q.B.D. 233.

(v) *Armstrong v. Jackson* (1917), 2 K.B. 822.

(w) *Williams v. Stevens*, L.R. 1 P.C. 352.

(x) *Salford Corp. v. Lever* (1891), 1 Q.B. 168.

(y) *Andrews v. Ramsay & Co.* (1903), 2

K.B. 635.

(z) *Boston Deep Sea etc. Co. v. Ansell* (1888), 39 Ch.D. 339.

(a) *Burland v. Earle* (1902), A.C. 83.

(b) *Heath v. Chilton* (1844), M. & W. 632.

(c) *Tennet v. Elliot*, 1 B. & P. 3.

(d) *Bholanath v. Mulchand*, 25 All. 639.

(e) *Henry Parker Ltd. v. Mason* (1940), 4 All E.R. 199.

(VII) An agent, in absence of a contract to the contrary, is not entitled to his *remuneration*, till the completion of the act, which he is employed to perform (sec. 219). Under the sec., however, the agent enjoys, as security for payment of such remuneration, the right to detain moneys received by him on account of goods sold, although all the goods have not been sold or the sale is not completed. If the agreement as to remuneration is in writing, the question depends on the construction of its terms.

In this connection, it has been held that an agent employed to "sell" property, is not entitled to his brokerage, till an actual sale is brought about (f). If the transaction goes off, after the parties have met, the broker loses his commission. Further, if an agent is employed as above, such employment does not prevent the principal from disposing of the property himself (f). Where an agent is employed for introducing a purchaser, who is prepared to offer the stipulated amount, the agent becomes entitled to the commission when he has introduced such purchaser, whether the transaction ultimately comes off or not (g). Similarly, where property is put in the hands of an agent to dispose of for the principal and the agent, having accepted the employment, has expended money and time in carrying it out, the principal is not entitled to withdraw the authority, at least after the agent has succeeded in finding a possible purchaser for it (f).

Whether the particular contract has been brought about by the intermediation of the broker is a question of fact. If he has brought together two contracting minds, who are able and willing to enter into the particular transaction, the broker has done what he was employed to do (h). It matters not that no contract immediately results. In a recent case before the Privy Council (i), a broker who was employed to introduce a purchaser for a particular quantity of coal, introduced one in December 1919. No transaction resulted then, though both parties were agreeable as regards the terms. In April 1920, however, two contracts (for larger amounts) were entered into between the same parties which contracts were found to be the result of the previous introduction. Held, the broker was entitled to his commission on both. If after a contract has been brought about, the principal refuses to complete the transaction, the broker is entitled to damages for the loss of commission which he would have earned (j).

An agent, however, who misconducts himself in the business of agency is not entitled to his remuneration for the part of the business he has misconducted, as laid down by sec. 220. Thus if the agent is employed to lay out Rs. 1,00,000 on good security and he lays out Rs. 90,000 on good and Rs. 10,000 on bad security, he is not entitled to any brokerage on the latter investment (see ill.).

Where several agents are employed, commission is not necessarily payable to the agent who first introduced the purchaser, but to the agent who was the effective cause of the sale (k). Notice that in some cases, commission may be payable even after the termination of the agency, e.g. where the agency is for an indefinite period and provides for the payment of commission on "repeat" orders (l). It may be payable even after the death of the agent, e.g. where the agreement provides for payment of com-

(f) Luxor Ltd. v. Cooper (1941), A.C. 108.

(g) Abdulla v. Animendra, 49 C.W.N. 621.

(h) Municipal Corporation of Bombay v. Cuverji Hirji, 20 Bom. 124.

(i) Valaraksha v. S. Coal Co. Ltd., 48

C.W.N. 1.

(j) Mehta v. Cassumbhai, 24 Bom. L.R. 847.

(k) Nightengale v. Parsons (1914), 2 K.B. 621.

(l) Levy v. Goldhill (1917), 2 Ch. 297.

mission so long as principal carries on business, with the customers introduced by the agent (m).

Agent's lien (sec. 221)

Under sec. 221, in absence of a contract to the contrary, an agent is entitled to retain goods, papers and other property, whether moveable or immoveable, of the principal received by him, till the amount due to him for (i) commission, (ii) disbursements and (iii) services in respect of the same has been paid.

This is called the *agent's particular lien*. It covers all property of the principal, which is received by the agent as such. The property must be received by him lawfully. It must not also have been received by him for a specific purpose. In such cases there is no lien. Lastly, the lien is for services, etc. rendered to the property in question and not to any other property. In a Bombay case (n), the secretaries and treasurers of a limited company claimed a lien under the sec. on the goods, papers and other property of the company in their possession for loans made by them to the company. *Held*, they had no such lien, as the loans had not been specially assigned to the property in question.

The lien is confined to the rights of the principal at the time in the property in question and is subject to all rights and equities of third persons existing against it at the time. The lien being possessory is lost, by loss or parting with the possession of the property or by the agent taking security from the principal in a manner showing a waiver of the lien (o).

A sub-agent properly appointed is entitled to the same lien against the principal, as he has against the agent and this lien is not affected by any settlement between the principal and the agent (p). A sub-agent improperly appointed has no such lien against the principal.

Principal's duty to agent (secs. 222-25)

These are : (i) under sec. 222, the principal is *bound to indemnify* the agent against the consequences of all lawful acts done by the agent in pursuance of his authority. Thus if A at Calcutta, under instructions from B at Bombay, agrees to sell goods to C at Lahore, and B fails to send the goods, A if sued by C for breach of contract, is entitled to recover from B, all damages and costs he has to pay C in C's suit (see ill.). The right of indemnity extends to losses or liabilities incurred by the agent in exercising his authority, according to the custom or rules of the market in which he is working.

Thus where C employed X as his agent to make speculative purchases of cotton on C's behalf and the prices of cotton having fallen, C became heavily indebted to X and thereupon X closed the transactions by selling the cotton he had bought for C, *held*, C was bound to indemnify X as X had incurred personal liability and as the sale of the cotton had resulted in a loss (q).

Where deposit of margin money is agreed to between the parties the adatia is entitled to close the transactions of the principal if the latter fails

(m) *Wilson v. Harper* (1908), 2 Ch. 370.

(n) *The Bombay Saw Mills Co.*, 13 Bom.

314.
(o) *In re Douglas* (1898), 1 Ch. 199.

(p) *Fisher v. Smith* (1878), 4 A.C. 1.

(q) *Christofordies v. Terry* (1942), A.C. 566.

to pay margin money demanded by the adatia. One general demand for margin for all outstanding transactions, however, or an excessive demand for margin, will not be justified (r). The right of indemnity is lost, if the agent acts negligently or beyond his authority (s). The present sec. deals with the lawful acts of the agent.

Sec. 223 deals with wrongful acts. Under it, (i) the principal is bound to indemnify the agent against the consequences of all acts done by the agent *bona fide* under the principal's instructions though such acts may cause injury to the rights of third persons. Thus if a decree-holder, in execution of his decree, instructs the Sheriff's officer to attach property belonging to a third person as the debtor's property and the officer has to pay damages for his act to the owner, he can recover the same from the decree-holder, though the act was wrongful. Notice that if the agent knows that the act is unlawful, he will lose his right under the sec. (t). Further, if the act is criminal, there is no right of indemnity at all (sec. 224), e.g. agency to commit an assault or to publish a criminal libel. (ii) Secondly, the principal is bound to compensate the agent for injuries caused to the latter, by the principal's neglect or want of skill (sec. 225), e.g. providing a bricklayer with a defective staircase.

Effect of agency on contracts with third persons (secs. 226-38)

Generally speaking, contracts entered into through an agent, and obligations arising from acts done by an agent may be enforced in the same manner and have the same legal consequences as if they were entered into or were done by the principal himself (sec. 226). This is so, where the agent acts within the scope of his authority. The principle does not apply if the agent's act is outside the scope of his authority. If the agent exceeds his authority, and what he does in excess can be separated from what is authorised, the principal, as between himself and the agent, is only bound by the latter and not by the former act (sec. 227). On the other hand, if what is done in excess cannot be separated from what is done within his authority, the principal, as between himself and the agent, is entitled so repudiate the whole (sec. 228).

Thus if A instructs B to buy one property and he buys that property and another, the principal is not bound to recognise the latter transaction, if the price paid for each is separate. If a single price is paid for both by the agent, the principal may repudiate the whole transaction.

Notice that the above rules apply only as between the principal and the agent. As regards third parties, the principal may be bound by an unauthorised act of the agent, if the act is within the ostensible authority of the agent and the third party has acted *bona fide* (u). Further, the fact that the agent has committed a fraud on the principal in doing an act which is authorised, will not make the act the less binding on the principal (v).

Notice to agent (sec. 229)

Under sec. 229, any notice given to or information received by an agent, in the course of business transacted by him on behalf of his principal, shall

(r) *Devshi v. Bhikhamchand*, 29 Bom. L.R. 147.

(s) *Davison v. Fernandis* (1889), 6 L.T.R. 73.

(t) *Re Parker* (1882), 21 Ch.D. 408.

(u) *Baincs v. Ewing* (1866), L.R. 1 Ex. 320.

(v) *Hambro v. Burnard* (1904), 2 K.B. 10.

have the same legal consequences, as between the principal and third parties, as if it had been given to or received by the principal. In other words, the rule is that knowledge of the agent is knowledge of the principal. This is irrespective of actual knowledge.

Thus where an insurance broker entered into a contract of insurance with a person who had lost an eye, it was held that the insurance company could not avoid the contract on account of want of full disclosure by the assured (*w*). Similarly, where the master of a ship failed to inform the shipowners of the fact that the ship had been damaged, a policy of insurance taken out by the latter, without disclosing the fact, was held void (*x*).

The agent must have received the notice in the course of the business of agency. Any notice received by him outside this, cannot be binding to the principal. Further, it must be the duty of the agent to communicate the fact to the principal. If there is no such duty in a given case, the sec. will not apply (*y*). Where an agent is acting in fraud of his principal, notice cannot be imputed to the principal, because in such a case, communication by the agent is extremely improbable (*z*). Notice to agent may be actual or constructive. Both are imputed to the principal under the sec. (*a*).

Agent, when personally liable (sec. 230)

The sec. provides that, in absence of a contract to the contrary, an agent cannot personally enforce contracts entered into by him on behalf of the principal nor is he personally bound by them.

That being the general rule, certain presumptions are raised in specified cases where such "contract to the contrary" shall be presumed to exist: e.g. (i) where a contract is made by an agent for a merchant resident abroad; (ii) where the agent does not disclose the name of the principal; and (iii) where the principal, though disclosed, cannot be sued. In these three cases, law raises a presumption that the agent was intended to be personally liable. It is a presumption, however, and can always be rebutted by suitable evidence to the contrary. Where an agent is personally liable on a contract, he himself can sue and be sued thereon.

An agent is personally liable: (i) where he enters into a contract so as to make himself personally liable thereon. Whether this is so in a given case, is a question of construction. Where a contract said "we the undersigned three of the directors agree to pay moneys advanced to the company," it was held that this created a personal liability as regards the directors (*b*). On the other hand, where a contract said "I undertake on behalf of A (principal) to pay", a certain sum of money and it was signed by the agent, as agent, it was held that the agent was not personally liable (*c*). The contract as a whole, along with the terms of the signature, must be construed (*d*).

In a Bombay case (*e*), the plaintiff had entered into a contract of service, which was headed as "Shire Highland Railway Co., Nyasaland, Ltd." under which he agreed

(*w*) Bowden v. London etc. Assurance Co. (1892), 2 Q.B. 534.

(*x*) Gladston v. King (1813), M. & W. 35.

(*y*) Blackburn v. Vigors (1877), 12 A.C. 531.

(*z*) Cave v. Cave (1880), 15 Ch.D. 639.

(*a*) Manchester Trust v. Furness (1895), 2 Q.B. 539.

(*b*) MacCollin v. Gilpin (1881), 6 Q.B.D. 516.

(*c*) Dowman v. Williams (1885), 7 Q.B. 103.

(*d*) Universal Steam N. Co. v. James MacKelvie & Co. (1923), A.C. 422.

(*e*) Ganpat v. Forbes Forbes Campbell & Co., 32 Bom. L.R. 1336.

to serve the said company in East Africa on certain terms. The contract ended with the words "for F.F.C. & Co. Ltd., J. Jenkins, Assistant Agents, Shire Highland Rly. Co., Nyasaland, Ltd." In a suit filed by the plaintiff for wrongful dismissal, against F.F.C. & Co. Ltd., in Bombay, as personally liable on the contract, *held*, negating the contention, that the agreement made it clear that plaintiff had intended to enter into the contract with the Railway Co. direct and that the signature, together with the use of the words "agents", made it plain that F.F.C. & Co. Ltd. were negating their personal liability.

Notice that an agent who has an interest of his own in the business of agency, e.g. a factor, or auctioneer, can always sue and be sued personally. This is because to that extent he is a principal. Further, an agent can also sue in his own name for recovery of money paid by him by mistake or by reason of fraud or other wrongful act of the other party or where the consideration has wholly or partly failed (f).

(ii) Where an agent acts for a foreign principal, the presumption is that credit has been given to the agent and not to the foreign principal. He can, therefore, himself sue and be sued on the contract. Where, however, the terms negative such presumption, the agent cannot be sued. Thus where the foreign principals were named in the contract and the agents were described as acting for such principals, the agents were held not liable (g). An English company having a branch office in India is a foreign principal. A contract entered into by the managing agents of such a branch is enforceable against such agents personally, unless the contract is made in the name of such foreign company (h). Notice that in England grave doubt has been expressed as to the existence and validity of the exception in the modern conditions of life (i).

(iii) The agent is also presumed to be intended to be personally liable where he acts for an "*undisclosed principal*". The principal being unknown, obviously, the credit must have been given to the agent in such cases and he, therefore, can be sued on such contract and he can himself sue thereon.

Thus the honorary secretary of a school in India, said to be conducted by a certain association in England, whose name was not disclosed, was held personally liable for rent of premises leased out by him in his own name (j). If, however, the other party knows that the agent is contracting as such, he cannot hold the agent personally liable, although he has not disclosed the name of the principal at the time the contract was made. Thus where a charter party was entered into between X as agent for the ship-owners and "J. M. & Co., Charterers" and was signed "for and on behalf of J. M. & Co. (as agents) J.A.M." and charges for demurrage having been incurred, the ship-owners filed a suit against "J. M. & Co.", it was held that "J. M. & Co." could not be made liable on the contract, as X knew when the contract was signed, that "J. M. & Co." were acting as agents for another, though the latter's name was not disclosed and though "J. M. & Co." were described in the contract as "charterers" (k).

Notice that in case of negotiable instruments, the agent's liability is always excluded, if he signs his name as agent (see sec. 28, Negotiable Instruments Act). If on a construction of the whole contract, the agent acting for an undisclosed principal, appears to have made himself personally liable, he is liable to be sued personally thereon. Thus where an agent

(f) Colonial Bank v. Exchange Bank (1885), A.C. 84.

(g) Ogden v. Hill (1879), 40 L.T. 751.

(h) Tutika v. Perry & Co., 27 Mad. 315.

(i) Miller Gibb & Co. v. Smith & Tyren

(1917), 2 K.B. 141.

(j) Bhojabhai v. Hayem Samuel, 22 Bom. 754.

(k) Universal Steam Navigation Co. v. James Macelvaine & Co. (1923), A.C. 492.

signed a bought note saying "bought of you for my principal", it was held that the agent was personally liable (l).

(iv) The last case in which the agent is presumed to be intended to be personally liable is when the principal, though disclosed, cannot be sued, e.g. in case of contracts entered into by agent for Sovereign States. Such States are not subject to civil process by International Law. The agent, in such case, therefore, is personally liable. An agent acting for a non-existing party, also may be personally liable, e.g. a solicitor acting for a client, who is already dead, or who does not in fact legally exist.

Notice that where an agent is entitled to sue personally on a contract entered into by him for his principal, his right will come to an end, as soon as the principal intervenes. Thus a settlement between the principal and third parties would be a good defence to an agent's suit in such cases. It is otherwise, when the agent has a lien on the subject-matter, e.g. an agency coupled with interest (m). Notice that as has been held in Bombay, where an agent by contracting, renders himself personally liable for the price of goods, bought on behalf of the principal, the property in the goods, as between the agent and the principal, vests in the agent and does not pass to the principal until he pays for the goods and the agent has the same rights as regards the disposal of the goods and to stop them in transit as he would have had if the relation between him and the principal had been that of seller and buyer (n).

Undisclosed principal disclosing himself (secs. 231-32)

Where a contract is entered into with a person without knowing or suspecting that he is an agent, the latter's principal can, in law, require performance of the contract from the other party. But if the principal does so, i.e. if "he discloses himself" before the contract is completed, the other party may refuse to perform the contract, if he can show that he would not have entered into the contract if he had known who the principal was or that the agent was not the principal. Further, where in such case, the principal requires performance of the contract, the other party will have the same rights against the principal as he would have had, if the agent was the principal.

The above secs. deal with a case where neither the existence nor the identity of the principal is disclosed at the time of entering into the contract, i.e. where the contract is with the agent believing him to be a principal. The concealed principal, in such a case, can demand performance from the other party, only on condition of allowing the other party the same rights against himself, as he had against the agent (o). Thus a set-off which the third party has against the agent can be availed of against the principal as also any equitable defences of a similar kind (p). The words "discloses himself" apply only in cases where the principal himself discloses his identity. They do not apply where the disclosure is made by some other person (q).

(l) *Southwell v. Bowditch* (1876), L.R. 1, C.P.D. 374.

(m) *Drinkwater v. Goodwin* (1775), Comp. 251.

(n) *Babasha v. Hombanna*, 34 Bom. L.R. 1268.

(o) *George v. Clagget* (1797), 7 T.R. 359.

(p) *Montague v. Forewood* (1893), 2 Q.B. 350.

(q) *Laxmandas v. Lane*, 6 Bom. L.R. 731.

Agents' liability (secs. 233-34)

Under sec. 233, when the agent is personally liable, the person dealing with him may hold either him or his principal or both of them liable. Generally speaking, an agent who contracts as agent cannot sue nor be made liable on such a contract. In certain cases, however (mentioned by sec. 230), the agent can be personally liable. In such cases, the other party has a double option: He can sue either the agent or the principal or both together, the only exception being the case contemplated for by sec. 233, viz. where the contract has been entered into on the understanding that either the agent alone or the principal alone will be regarded as liable in respect of it (r). In such cases, no other party can be subsequently held liable thereon. In other words, under sec. 230 where it applies, the liability of the agent and principal is alternative. The result is that when a creditor has once sued the agent to judgment, he has no remedy left against the principal, if the judgment obtained by him against the agent remains unsatisfied. And this is so, even though he was not aware of the existence of the principal, at the time when he sued the agent (s). Of course, if the suit against the agent is dismissed, his rights to proceed against the principal will remain unaffected (t). Notice that law requires the third party to make his election within a reasonable time after knowing who the principal is.

Agents' warranty of authority (sec. 235)

Under sec. 235, if a person untruly represents himself to be the agent of another and thereby induces the third person to enter into a contract with him, he is liable to make good to such person, the loss caused to him, if his alleged employer does not ratify the act. The liability created by the sec. is in tort and not on contract and is based on the breach of an implied warranty of authority (u). It applies not only where a person untruly represents himself as agent, but also when, being in fact an agent, he exceeds his principal's authority. It is immaterial that the agent made the false representation innocently.

In an English case (v), solicitors had been instructed by a client to defend a threatened suit. Before proceedings started, the client became a lunatic. The solicitors, in ignorance of the fact, took steps in defending the proceedings. Held, they were personally liable for the other side's costs, as on a breach of a warranty of authority. In another English case (w), a broker, *bona fide* relying on a power of attorney purporting to be signed by two trustees of a certain stock, standing in their joint names with the Bank, induced the Bank to transfer the same to a buyer. It turned out that the signature of one of the trustees was forged. Held, the broker, having warranted his authority to transfer the stock to the Bank, was liable to indemnify the Bank against the claim of the co-trustee for restitution.

The measure of damages, which the agent in such cases is bound to pay is the actual loss sustained. Thus if the directors of a company issue debentures without authority, the measure of damages payable by them to the debenture holders will be the full value of the debentures. It would, of

(r) *Babulal v. Jagat Narayan*, A.I.R. (1952) V.P. 51: See, however, *Nicholas v. Nimazec*, A.I.R. (1952) Cal. 859.

(s) *Shivlal v. Birdichand*, 19 Bom. L.R. 370.

(t) *Curtis v. Williamson* (1874), 10 Q.B.

57.

(u) *Collen v. Wright* (1875), 8 E. & B. 647.

(v) *Young v. Toynbee* (1910), 1 K.B. 215.

(w) *Starkey v. Bank of England* (1903), A.C. 114.

course, be otherwise, if the company was insolvent and the debentures were not worth anything at all.

Pretended agent (sec. 236): Under this sec., a person with whom a contract is entered into as an agent, is not entitled to require performance of it, if in reality, he was acting, not as agent, but as principal. In other words, a pretended agent cannot sue to enforce the contract by subsequently coming out as the principal. It has also been held that when a person enters into a written agreement, calling himself the "sole principal", another person cannot be allowed to sue on the contract as an undisclosed principal (x).

Agency by holding out (sec. 237)

Under sec. 237, when an agent, without authority, has done acts or incurred obligations to third persons, on behalf of his principal, the principal is bound by such acts and obligations, if he has by words or conduct, induced such third persons to believe that such acts and obligations were within the scope of the agent's authority. This is called "*agency by holding out*" or "*agency by estoppel*".

The principle is that if a person by his conduct, represents to another that a certain state of facts is true, he is bound in law by such representation, if the other party acts on the same, to his prejudice. Thus if a person employs an auctioneer to sell goods on his behalf, and privately instructs him not to sell below a fixed price, a sale by him below the fixed price will be binding on the owner, if the purchaser purchased the goods, *bona fide*, without notice of the reservation. Similarly, where a charter party provided that the master (who was appointed by the shipowner) should sign bills of lading as agent of the charterers only, it was held that the shipowners were liable on bills of lading signed by the master in favour of persons who had no notice of the charter party (y). Notice that under the sec., the principal is liable only if the other party was unaware of the fact of the agent's want of authority. The act also must be the act of the agent, in the course of his employment as agent for the principal. An act done, otherwise than in the course of such agency, does not come under the sec. (z).

Principal's liability for fraud of agent (sec. 238)

Under sec. 238, misrepresentations made and frauds committed by agents, acting in the course of their business for their principals, have the same effect on agreements made by such agents as if such misrepresentations or frauds had been made or committed by the principal, but misrepresentations made and frauds committed by the agents, in matters which do not fall within their authority, do not affect their principals.

The principle underlying the sec. is the same as underlying sec. 226; as contracts made by agents within the scope of their authority bind the principals, so also, frauds committed and misrepresentations made by agents, in matters within their authority bind their principals. The crucial question always is: is the act (viz. fraud or misrepresentation) done by the agent in the course of business authorised by the principal? If it is, the act binds the principal, though the principal may not have actually authorised the particular act, e.g. if a landlord employs a rent collector to collect the rents,

(x) *Humble v. Hunter* (1848), 2 Q.B. 310.
(y) *Manchester Trust v. Furness* (1895), 2 Q.B. 539.

(z) *Macgowan v. Dyer* (1873), L.R. 8 Q.B. 141.

a payment of rent made to such person is binding on the landlord, though the rent collector has actually misappropriated the moneys himself. In other words, the fraud must have been committed by the agent while acting in the course of his actual or ostensible authority. Notice that it has been now settled that it makes no difference to the application of the above rule that the agent has committed the particular fraud, for his own benefit or for the benefit of the principal (a).

In the last case, a solicitor's managing clerk, who had authority to transact conveyancing business on behalf of his master, fraudulently induced an old and ignorant lady client, to sign a conveyance of her own properties (which she had instructed the solicitors to sell) in favour of himself. With the help of these documents, he subsequently sold the properties as his own and absconded with the sale proceeds. In a suit by the client, the solicitors were held liable to make good the loss caused to their client by the fraudulent acts of their agent. On the other hand, the master of a ship has no authority to sign bills of lading, without goods being actually put on board. A master's act therefore (even if fraudulent), in signing such bills of lading, without goods being placed on board, is not binding on the principal because it is done in the course of an employment which is not authorised (b). Similarly, a company's secretary issuing a fraudulent and forged share certificate, will not bind the company, because it is not within the secretary's authority to issue a certificate (c). Notice that in absence of actual fraud or dishonesty on the part of the principal, knowledge by him of facts which render a statement innocently made by the agent false, does not make the principal guilty of fraudulent misrepresentation, so as to avoid the contract entered into by the agent (d).

In this case an agent made an innocent mis-statement about the value of a property he was offering for sale on behalf of the principal. The principal knew the correct facts but had not deliberately withheld them from the agent nor had he authorised the agent to make the false statement in question. In fact, he did not know that the agent was making such statement. The purchaser agreed to purchase the property on the basis of the agent's representations. *Held*, the purchaser could not claim damages against the principal on the ground of fraudulent mis-representation.

CHAPTER X

SALE OF GOODS

HISTORICAL RETROSPECT: The "Indian Sale of Goods Act" (III of 1930) was passed by the Indian Legislature in 1930. The Act repealed Ch. VII of the Contract Act, which originally dealt with sale of goods. It received the assent of the Governor-General on 15th March 1930 and became operative as law from 1st July 1930 [sec. (1) (3)]. It extends to the whole of India, except Jammu and Kashmir [sec. (1) (2)]. Though old Ch. VII of the Contract Act is repealed by this Act, the other unrepealed provisions of the former Act, as far as they are not inconsistent with provisions of this Act, continue to apply (sec. 3). The Act is a defining and amending Act (see preamble). It is therefore not permissible, while constructing the Act, to consider what the law previously was, the language of the Act itself must be examined first and it is only when the meaning appears doubtful that regard can be had to earlier legislation (e). The Act is not retrospective (sec. 3). It does not affect rights, interests, obligations and titles acquired or which accrued before the commencement of the Act (see sec. 66).

(a) *Lloyd v. Grace Smith & Co.* (1912), A.C. 716.

(b) *Grant v. Norway* (1851), 10 C.B. 665.

(c) *Reuben v. Great Fingall etc.* (1906), A.C. 439.

(d) *Armstrong v. Steain* (1952), 1 All E.R. 139.

(e) *Bank of England v. Vagliano* (1891), A.C. 107.

Definitions (sec. 2)

This sec. defines various terms which are used in the body of the Act. Some important definitions are considered :

(i) **"documents of title to goods"** (cl. 4): These are certain documents, which are regarded in the ordinary course of trade and commerce as equivalent to (i.e. as proof of) the possession (or control) of the goods represented by them or which authorise the possessor of such documents (by endorsement or delivery) to transfer or receive goods represented by them. The clause mentions some of such documents, e.g. bill of lading, dock warrant, warehouse-keeper's certificate, wharfinger's certificate, railway receipt, warrant or order for delivery of goods (generally called "delivery order" or D/O). The list is not exhaustive. Any other document which has the above characteristics will also fall under the same category. Though a bill of lading is a document of title, a mate's receipt is not; it being regarded in law as merely an acknowledgment of the receipt of the goods (f).

The importance of "documents of title" lies in the fact that they enable their holders to deal with goods represented by them by way of sale or otherwise, as the exigencies of business require, although the goods themselves may not, in fact, be in their possession, e.g. when they are still on the high seas, in course of transmission to them. Thus they simplify commerce. These "documents of title" are regarded in law as equal to goods themselves and therefore they can be transferred from one person to another in the same way as goods can be. If the documents are drawn in favour of bearer, they are transferable by delivery; if "to order", by endorsement and delivery. Sometimes, the possession (legal or otherwise) of these documents creates difficulties, e.g. where a mercantile agent who has been given these documents by the rightful owner, in ordinary course of business for a particular purpose, abuses the trust and uses the documents for his own purposes and misappropriates the proceeds thereof, e.g. by effecting a sale of the goods, as if they were his own. These difficulties are considered and provided for in secs. 27-30, and 53 of the Act (see seq.).

(ii) **"Goods"** (cl. 7) are defined to mean every kind of moveable property other than actionable claims and money. This is a wider definition than one obtaining in English Law. They include stocks and shares (which are not considered "goods" in England), growing crops and things attached to or forming part of land, e.g. growing trees or machinery fixed or embedded in earth, which are agreed to be severed before sale or under the contract of sale.

"Actionable claims" are claims which can be enforced only by an action or a suit, e.g. a debt. A debt is not moveable property or goods. Provision for transfer of such "actionable claims" is made by the Transfer of Property Act.

The importance of this definition lies in this that only those things which can be legally called "goods" are governed by the provisions of this Act. Sale of immoveable property is not governed by this Act, but by the Transfer of Property Act.

(iii) **"Future goods"** (cl. 6): These are goods to be manufactured or produced or acquired by the seller after the making of a contract of sale.

Under the Act, a contract for the sale of future goods, e.g. 100 tons of rice to be grown on A's field, is not illegal, though an actual sale of future goods is not permissible (see sec. 6).

(iv) "**Mercantile agent**" (cl. 9): This is a technical expression and is taken from the English Factors Act of 1889. It is used to denote a special kind of agent, i.e. "an agent having, in the customary course of business as such agent, authority either to sell goods or to consign goods for purposes of sale or to buy goods, or to raise money on the security of goods". In other words, he is an agent with an authority from the owner, either express or implied, to deal with the goods in his possession in his own name, by way of sale or pledge or otherwise. Examples of such kind of agents are auctioneers, factors, brokers, etc. A servant or a caretaker, on the other hand, is not such an agent, because he has no authority from the owner to deal with or dispose of the goods.

The importance of this definition lies in the fact that such agents, having by virtue of their authority, power to dispose of the goods belonging to another, are in the position of ostensible owners. Any dealing with the goods by them, in breach of their authority, therefore, will give rise to difficult questions between innocent transferees and the real owners. These questions are considered and provided for in secs. 27-30 of the Act.

(v) **Delivery** (cl. 2) means the voluntary transfer of possession from one person to another. It may be either (a) *actual* or (b) *constructive*. In (a) physical possession is transferred by one person to another. In (b) though the actual physical possession is not transferred, it is deemed to be so transferred, by the operation of a rule of law, e.g. where a warehouseman holding the goods of A, agrees to hold them on behalf of B, at A's request. This is, in law, called "*attornment*". There is still another kind of delivery which is called "*symbolic*". In this, instead of there being an actual physical transfer of the goods, something which gives the power to control such transfer is given by one person to another, e.g. handing over the key of a godown, transfer of a bill of lading. This is good delivery in law, of the goods in the godown or on the ship, as the case may be. "Forward delivery" means delivery in future (g).

(vi) "**Specific goods**" (cl. 14) means goods identified and agreed upon at the time the contract of sale is made. This definition is to be contrasted with that of "future goods" mentioned above. "Ascertained goods" has been held to mean goods identified in accordance with the agreement after a contract of sale has been made (h).

(vii) "**Deliverable state**" (cl. 3): Goods are said to be in a "deliverable state" when they are in such a state that the buyer would, under the contract, be bound to take delivery of them, e.g. when the contract is to sell timber growing on A's land and A is bound under the contract to cut the timber and make bundles thereof, the goods will be in a "deliverable state", when A has done the above things. Under sec. 21, where the seller has, under the contract, to do something to the goods to put them into a deliverable state, the property does not pass to the buyer till he has done so. It should be observed that expressions used but not defined in the Act but

(g) *Pragdas v. Jiwanlal*, A.I.R. (1948), A.C. 217.

(h) *Re Wait* (1927), 1 Ch. 606.

defined in the Indian Contract Act have the same meaning as is assigned to them in the latter Act (cl. 15).

Contract of Sale and Sale distinguished (sec. 4)

Cl. 1 of sec. 4 defines a contract of sale of goods as "a contract whereby the seller transfers or agrees to transfer the property or goods to the buyer for a price". It is distinguished from a sale, in the following particular: a sale involves a transfer of property in the goods from the seller to the buyer; in a contract of sale, no property in the goods is transferred to the buyer, but only a personal right is created in the buyer to sue for damages for breach of contract, if the agreement is broken by the seller.

The distinction is important from many points of view: (i) where the transaction amounts to a sale, a subsequent loss or destruction of the goods falls on the buyer (sec. 26). It is otherwise, where the transaction only amounts to an agreement of sale. (ii) Where there is only a contract of sale, the goods remain the seller's, so long as the property in them has not passed to the buyer. They can, therefore, be disposed of by the seller and they can also be attached in execution of a decree against the seller, which cannot be done if the transaction amounts to a sale. The test to determine whether a particular transaction amounts to a sale or a contract of sale, is laid down by cl. 3 of the sec., viz. to find out whether the property in the goods is transferred from the seller to the buyer under the contract. If property is transferred, it is a sale, though it may be called a contract or agreement of sale. Rules for determining when property is to pass, are laid down by secs. 18-26 of the Act. The present sec. (cl. 3) merely lays down a general rule that where the transfer of the property in the goods is to take place at a future time or subject to some conditions to be thereafter fulfilled, the contract is called an agreement to sell. It will become a sale when the time elapses or the conditions are fulfilled (cl. 4).

Sale and Contract for work and labour

These two are sometimes difficult to distinguish, e.g. where gold is supplied to a goldsmith for preparing an ornament. The test generally applied (i) is that if as a result of the contract, property in an article is transferred to one who had no property therein previously, for a money consideration, it is a sale, e.g. a painter to whom materials are supplied for painting a picture, which he agrees to paint for the supplier for a certain sum. Where it is otherwise, e.g. in case of the goldsmith above, it is a contract for work and labour. The distinction becomes important when questions of passing of property arise for consideration. The above-mentioned test however is a rough and ready test and is not universally applicable (j). A contract with retail furriers for a mink jacket for a price, skins, colour and style being chosen by the customer, was held not to be a contract for work and labour but for sale of an article for a price (k). A contract to make artificial teeth for a customer is held to be a contract of sale (l).

(i) *Lee v. Griffin* (1861), 30 L.J.Q.B. 252.
(j) *Dixon v. London Small Arms Co.*
(1876), 1 A.C. 632.

(k) *J. Mariot Ltd. v. Tapper* (1953), 1
All E.R. 15.
(l) *Lee v. Griffin*, 4 L.T. 546.

Sale and Hire Purchase

A transaction of sale has to be distinguished from another, apparently similar but different transaction, called "hire purchase agreement". In the case of the latter, the agreement between the parties in substance is to the effect that if the "hirer" regularly "pays" the various instalments agreed to between the parties, the subject-matter of the hire, e.g. a motor car, on payment of the last instalment, shall become the property of the "hirer" but that if such instalments are not paid, the article shall remain the property of the transferor and he shall be entitled to re-take possession thereof from the "hirer" without paying any compensation to him therefor. A hire purchase agreement, therefore, is both a bailment and an agreement to sell, which becomes an absolute sale on certain conditions being fulfilled.

Difficult questions arise as to the true construction and effect of such agreements. Sometimes the terms evidencing the transaction create an absolute sale, though in the document the transaction is called a hire purchase agreement. The test which is applied is, does the agreement give to the "hirer", an option to terminate the agreement by refusing to pay further instalments if he so desires? If it does, the transaction is an agreement of "hire purchase". On the other hand, if, by the terms of the agreement, the "hirer" is bound to pay all the instalments as agreed and is further not entitled to terminate the agreement at his choice, it is a contract of sale, though called a hire purchase agreement by the parties.

Thus in *Bhimji v. Bombay Trust Corporation (m)*, the plaintiff had purchased a car and paid a portion of the price. The balance of the price was paid by the defendant company, in whose favour the plaintiff passed a "hire purchase agreement" for the car. The agreement provided that the plaintiff was to repay the amount to the defendant company in stated monthly instalments and that on failure to pay any instalment, the defendant company were entitled to terminate the hiring and had the right to take the car into their possession. It was also provided that the plaintiff had the option of paying the whole amount at once before time, and that the car became his property, either when such option was exercised or all the instalments paid. During the currency of the agreement, the plaintiff was to hold the car as bailee for the company, and was not to have any property or interest as purchaser in it until he exercised his option of purchasing. The plaintiff paid the first three instalments though not regularly. The fourth was not paid on the due date. The defendant company, after notice to the plaintiff, took possession of the car. The plaintiff first offered to pay the instalments due and later offered to pay the whole balance of the price agreed. The defendants, however, declined to accept either proposal and eventually sold off the car. The plaintiff having sued to recover the car or its value or the balance of its sale proceeds, it was held that, as under the agreement, there was no option to the plaintiff to return the car to the defendant company after payment of one or more instalments and as he was bound to pay the whole amount according to the stipulated instalments, there was a sale of the car for consideration, payment of which was obligatory on the plaintiff and that, therefore, the sale of the car by the defendants was wrongful and amounted to conversion, for which they were liable to the plaintiff in damages.

A hire purchase agreement differs from an agreement to sell. In the former, there is no absolute sale, the person having the chattel is under no obligation to purchase and has the option of returning it at any time before all the instalments are paid. In the latter, the property in the chattel passes immediately to the purchaser on part payment and delivery (n). A penalty clause in a hire purchase agreement, e.g. that on failure to pay any instalment, the article shall belong to the owner and the hirer shall be

(m) 22 Bom. L.R. 64.

(n) *Cole v. Nanalal*, 26 Bom. L.R. 880.

bound to pay as damages a sum total of all the remaining instalments can be relieved against by the Court as being a penalty (o).

Conditional contracts

A contract of sale may be absolute or conditional (sec. 4, cl. 2). Conditions may be either *precedent*, *concurrent* or *subsequent*. In the first case, no obligation attaches under the contract unless the condition is first satisfied, e.g. where agreement of sale is as regards goods "to arrive", no liability arises under the contract, until the goods "arrive". In the second case, the performance of the condition must accompany performance of the contract, e.g. agreement to sell goods, cash against delivery. In the last case, on the specified condition happening or not happening as the case may be, the contract as already made, stands dissolved, e.g. where goods are sold with a condition that if the price is not paid as agreed, the contract shall be treated as cancelled.

Where there was a contract for sale of parachute cloth, January-February shipment, "the goods to be given delivery of when they arrive", held, the last words referred to the performance of the contract and did not make the contract conditional at its inception (p).

Contract of sale, how made (sec. 5)

A contract of sale may be made, as the sec. provides, by an offer to buy or sell goods for a price and the acceptance of such an offer. The contract may provide for an immediate delivery of the goods or for the immediate payment of the price or both or for delivery or payment by instalments or that delivery or payment or both may be postponed (cl. 1).

Cl. (2) of the sec. further provides that subject to any special law in force (e.g. the Transfer of Property Act, in case of sale of land), a contract of sale of goods does not necessarily require writing in order to be valid but may be made wholly or partly in writing or by word of mouth or by both or may be implied by conduct of the parties. In this, the Indian Sale of Goods Act makes a departure from English Law, which by sec. 4 of the English Sale of Goods Act, 1893, requires writing for certain kinds of contract, e.g. contract of sale of goods of the value of £10 or upwards, in order to make them enforceable at law.

A contract of sale may also be implied by conduct, e.g. where a person picks up a price-marked article in a shop with a view to purchase it.

Where a contract of sale is partly in print and partly in handwriting, the general principles applied are: (i) that the document as a whole, i.e. both the written and the printed portions, should be construed and as far as possible, full effect should be given to the whole (q). (ii) In case of a conflict or doubt, however, the written part should be given greater weight than the printed one (r). (iii) Where words in a printed form of a mercantile contract are deleted, the effect is the same, as if the deleted words had never formed part of the print at all (s).

(o) Cooden Engineering Co. v. Stanford (1952), 2 All E.R. 915.

(p) Ranchhoddas v. Nathumal, 51 Bom. L.R. 491.

(q) Mohanlal v. Krishna Premji, 30

Bom. L.R. 415.

(r) Paul Bier v. Chhotatalal, 6 Bom. L.R. 948.

(s) Sassoons & Sons v. International Banking Corp., 29 Bom. L.R. 1181.

Subject-matter of Contract (sec. 6)

Goods whether "*existing*" or "*future*" can form the subject-matter of a contract of sale. It is no objection to the validity of such a contract that the seller has purported to sell goods which are not in his possession, which do not belong to him or which are not then even in existence, e.g. an agreement to sell future crops of a particular field.

As cl. (2) of sec. 6 points out, however, *there cannot be a "sale" of future goods*. Such a "sale" in law, operates only as an "agreement to sell", with the result that property in the goods will pass from the seller to the purchaser only when the goods are produced and are unconditionally appropriated by the seller (or the buyer) to the contract, with the consent of the other party (see seq.). It is to be noted, however, that though an agreement to sell future goods does not at once pass property in the goods to the purchaser, it will operate in law, as an equitable assignment of the goods in question, the moment the goods are produced. The result is that a subsequent sale of the same goods to another, with notice of the first contract, will not defeat the title of the first purchaser (t). A transferee of the legal interest for value without notice, however, will acquire a good title to the goods as against the prior purchaser (u).

A contract of sale is valid even if the acquisition of the subject-matter of the contract by the seller is dependent on the happening of a contingency which may or may not happen (cl. 2). Thus a contract for sale of certain cloth to be manufactured by a certain mill, is a valid contract. If the particular mill does not manufacture the cloth, the contract becomes void (v). Such contracts are called "*contingent contracts*" (see secs. 31-36 of the Contract Act). Whether in a given case, the contingency has happened or not, is, of course, a question of fact, depending upon the terms of the contract.

Destruction of subject-matter of contract (secs. 7-8)

The above secs. lay down the rules applicable to cases where the subject-matter of a contract of sale is destroyed before and after the contract (cp. sec. 56 of the Contract Act). (1) Under sec. 7, *if at the time* the contract of sale is entered into, the subject-matter of the contract, being specific goods, has, unknown to the seller, perished or is so damaged as not to answer the description in the contract, the contract is void *ab initio*. If the seller was aware of the destruction and still entered into the contract, the law is that he would be estopped from disputing the validity of the contract (w).

Thus where 700 bags of nuts lying in particular warehouse were agreed to be sold, and it was found that unknown to both parties, 109 bags had been stolen from the warehouse before the contract was made, *held*, the agreement was void and the purchaser could not be compelled to accept the balance (x).

(2) Similarly, under sec. 8, where there is an agreement to sell specific goods and the goods *subsequently*, without any fault of the seller or buyer,

(t) *Holroyd v. Marshall* (1862), 10 H.L.C. 191; *Tailby v. Official Receiver* (1888), 13 A.C. 533.

(u) *Joseph v. Lyons* (1885), 15 Q.B.D. 280.

(v) *Bishweshwar v. Jaydayal*, 49 C.W.N. 368.

(w) *Smith v. Hughes* (1871), L.R. 6 Q.B. 597.

(x) *Barrow Lane, etc. Ltd. v. Phillips & Co. Ltd.* (1929), 1 K.B. 574.

perish or suffer such damage as not to answer their ^{an} (k) description in the contract, the agreement becomes void.

Thus where a certain quantity of wheat was sold by A to B and after the contract but before delivery to B, the goods were requisitioned by the Government, *held*, the contract was avoided (y).

It should be noted, however, that sec. 8 applies only "before the risk has passed to the buyer". This has reference to sec. 26, which lays down when risk passes from the seller to the buyer. Generally speaking, "risk passes with property", i.e. when property in the goods sold has passed to the buyer, the buyer takes the risk of subsequent destruction of or damage to goods. Sec. 8 applies both in case of a sale as well as an agreement to sell. It does not, however, apply to a C.I.F. contract, which is a contract for sale of goods "lost or not lost" (z) (see seq.). The words "not answering their description under the contract" mean that they are no longer "merchantable", as such goods, e.g. a cargo of Manilla hemp being accidentally so damaged by sea water that no one in the market will accept it as Manilla hemp (a) (see seq.). Thus the sec. covers deterioration of goods also, provided it is such as to make goods "unmerchantable".

Price (secs. 9-10)

"Price" means "the money consideration for sale of the goods" (sec. 2, cl. 6). Secs. 9 and 10 lay down *how price is to be fixed* at law. According to sec. 9, the price may be: (1) either fixed by the contract or (2) may be agreed to be fixed in a manner provided by the contract, e.g. by a valuer, or (3) it may be determined by the course of dealings between the parties. If it is not capable of being fixed in any of the above ways, (4) the buyer is bound to pay reasonable price. What is reasonable price is a question of fact in each case.

With reference to (3) above, sec. 10 lays down two additional rules: (i) if in such a case the valuer fails to fix the price, the contract is void, except as to part of goods delivered and accepted, as regards which the buyer is bound to pay a reasonable price. (ii) If in such a case any one of the two parties prevents the valuer from making the valuation, he shall be liable in damages to the other party. "Price" is an integral part of a contract of sale. If it is not fixed and is not capable of being fixed, the whole contract is void *ab initio*.

A "valuer" is to be distinguished from an arbitrator. The latter occupies a semi-judicial position. His "award" is a semi-judicial pronouncement. A valuer is a person who is appointed to value a thing because of his special skill, aptitude or knowledge. If appointed by the consent of parties, his decision, e.g. as to price, will be binding on the parties.

Custom or duty: Notice that where, after the price is fixed, a new or increased custom or duty is imposed before the goods are delivered and the seller has to pay it, the latter is entitled to add the same to the price. If the rate of custom or duty is lowered or removed, the buyer would be entitled to a reduction in the price (sec. 64A).

(y) *Shipton Anderson & Co. v. Harrison Bros.* (1915), 3 K.B. 676.

(z) *Manbre Saccharine Co. v. Corn Pro-*

ducts Co. (1919), 1 K.B. 198.

(a) *Jones v. Just* (1868), L.R. 3 Q.B. 197.

Rate of Exchange: Where price is payable in foreign currency, the exchange rate on the date fixed for payment is taken as the basis of conversion; in case of breach, the rate of exchange of the date of breach (b).

Conditions and Warranties (secs. 11-17)

Secs. 11-17 deal with the question as to the legal effect of various terms in a contract of sale, and the legal consequences of a breach of any one or more of them. All terms of a contract are not on the same footing. Some may be intended by the parties to be of a fundamental nature, e.g. quality of the goods to be supplied, the breach of which, therefore, will be regarded as a breach of the whole contract. Some may be intended by the parties to be binding, but of a subsidiary or inferior character, e.g. time of payment, so that a breach of these terms will not put an end to the contract but will make the party committing the breach, liable in damages. The former are called by sec. 12 "*conditions*", the latter are called "*warranties*".

A "*condition*" has been defined by sec. 11, cl. (2), as "a stipulation essential to the main purpose of the contract, the breach of which gives rise to a right to treat the contract as repudiated". A "*warranty*", on the other hand, has been defined by cl. (3) as a "stipulation collateral to the main purpose of the contract, the breach of which gives rise to a claim for damages but not to a right to reject the goods and treat the contract as repudiated". The implications of the above definitions are that if a party to a contract commits a breach of a term which the law regards as a "*condition*", this would amount to a breach or repudiation of the whole contract by the party in breach, thus giving the opposite party all rights which in law arise on such total repudiation, e.g. a right to reject the goods or a right to refuse to pay the price. On the other hand, if the term which is broken amounts only to a "*warranty*", both the parties remain bound to perform their respective parts of the contract, e.g. to give and take delivery or to pay the price, etc., the only right accruing to the party against whom the warranty has been broken being to claim damages from the other for any loss which may arise from the breach of the "*warranty*".

How distinguished: Sec. 12, cl. (2), lays down *two rules* for the purpose: (i) whether a stipulation in a contract of sale amounts to a "*condition*" or a "*warranty*" depends entirely on the construction of the terms of the contract. (ii) A stipulation may be a "*condition*" though called a "*warranty*" in the contract. In other words, it depends entirely on the intention of the parties, as evidenced by the terms of the contract, whether a particular term is a "*condition*" or "*warranty*"; the name given to it in the contract itself being, for this purpose, quite immaterial.

Representations: "*Conditions*" or "*Warranties*" are to be distinguished from what are called "*representations*", which generally precede the making of a contract and sometimes also accompany it. They do not form part of the contract and generally do not give rise to any legal liability, in case they are broken. If, however, the representations have induced the other party to enter into the contract, a case of avoiding the whole contract may arise under secs. 17 and 18 of the Contract Act, on the ground of either fraud or misrepresentation. They may also amount to "*warranties*" or "*conditions*", in proper cases. Beyond this, it does not appear that representations have any special legal effect.

Consequences of breach of "condition" and "warranty"^{an} (sec. 13)

Sec. 13 defines the legal consequences which result where a condition or warranty is broken. When a contract is subject to a condition to be fulfilled by the seller, the buyer may, on *breach of such condition*:

(i) Treat the contract as repudiated and claim damages on the footing that the whole contract is broken (sec. 12, cl. 2).

(ii) He may also waive the condition, and require the other party to go on with the performance of the contract (sec. 13, cl. 1).

(iii) He can also elect to treat the breach of condition as a breach of warranty, and claim damages on that footing (*ibid*). In such a case both parties will remain bound to perform their respective parts of the agreement, the right of the party suffering by breach of the condition being to claim damages for loss caused by that particular breach.

(iv) In certain cases the buyer is compelled, by a rule of law, to treat the breach of a condition, as a breach of warranty and to adjust his claims against the seller accordingly. These cases are: (a) where the contract is not severable and the buyer has accepted the goods or a part thereof; (b) where the contract is for specific goods and the property therein has passed to the buyer. In these two cases, the seller, though in fact guilty of a breach of condition, can be held liable by the buyer for a breach of warranty only (cl. 2, sec. 13).

(v) Where the performance of a condition or warranty is excused by law, as being impossible, no liability shall attach for its breach (sec. 13, cl. 3).

Where a *warranty is broken*, (i) the contract cannot be treated as repudiated by the other party; (ii) the right of the party suffering by its breach, is to claim compensation from the other, for such loss as directly results from its breach (sec. 12, cl. 2).

Cases under (iv) above arise, when the buyer having taken delivery of part of the goods, finds that a condition (e.g. as to quality) has been broken or where before taking delivery, he has exercised acts of dominion over the goods, e.g. has re-sold the goods to a third party. In all such cases, the buyer can treat the breach of condition as breach of warranty only and cannot therefore rescind the contract (c). Notice that there must be a positive act on the part of the buyer, before a breach of condition by the seller can be said to have been "waived" by the buyer, e.g. receiving the benefit of performance from the seller after knowing of the breach of condition on his part.

Under the second cl. of sec. 13, the "waiver" on the part of the buyer of breach of condition by a seller is a compulsory waiver, when the conditions of the cl. are satisfied.

Thus where on the sale of wheat the buyer took up the documents and delivered part of the wheat to a sub-buyer without inspecting the quality and the quality was thereafter found to be defective, *held*, the buyer had lost the right to refuse the goods (d). Similarly, where a buyer without examining the goods put his marks on them, *held*, he was not entitled to reject them on the ground that the goods did not answer the description of the contract (e).

(c) Nagardas v. Velmahomed, 32 Bom. L.R. 454.

(d) Hardy v. Hillers (1923), 2 K.B. 490.
(e) Nagardas v. Velmahomed (*supra*).

Im R 1. "conditions" and "warranties" (secs. 14-17)

Conditions and warranties may be either (i) *express* or (ii) *implied*. They are "express" when the terms of the contract expressly provide for them. They are "implied", when not being expressly provided for, the law implies them in any particular contract by operation of its own rules.

An *express condition or warranty* may be of any kind that the parties may choose to agree upon, e.g. an agreement to sell goods with a condition that the buyer shall not sell it below a certain minimum price; that the delivery shall be taken on or before a certain day, that the goods shall be what is called "fair Bengal cotton". On the other hand, a contract for the sale of a horse as "sound", is a contract with an *express warranty* of "soundness". Notice in this connection that as sec. 11 provides, a stipulation in a contract as to *time of payment* is not to be regarded as, a stipulation in law as "of the essence of a contract" of sale, unless the terms of the contract show a contrary intention.

Thus where a specific quantity of oats was sold by A to B, to be paid for by a particular date, and B failed to pay the price on the agreed date, held, on A refusing delivery to B on B's subsequent tender of the price, that A's action was not justifiably and that A's subsequent re-sale of the goods was also bad in law (f).

As regards other stipulations as to time (e.g. of delivery), it depends on the terms of the contract, whether they are to be treated as "of the essence" or not. Notice that as noted earlier, in a contract for the sale of goods, stipulations as to time of performance are presumed to be of the essence of the contract, e.g. date of shipment, date of loading, date of clearance (g). Where time is of the essence of a contract for sale of goods, the seller is entitled to put an end to it on the buyer's default, even though the property in the goods has passed to the buyer (h).

As regards *implied conditions and warranties* they are provided for by secs. 14-17 of the Act. They are, by law, incorporated in every contract of sale of goods, unless the terms of the contract show a contrary intention. The implied conditions and warranties provided for by the Act are as follows:

"Condition" as to Title

(I) Under sec. 14, cl. (a), in every contract of sale of goods, subject to a contrary intention appearing, there is an *implied condition* that the seller has a right to sell the goods and in case of an agreement of sale, that he shall have the right to sell, at the time when property is to pass. This is called "*condition as to title*". Thus where A purchased a motor car from B and after using it for some time, he was compelled to return it to the true owner, it appearing that B had obtained the car by theft, it was held that B had broken the condition as to title and A was therefore entitled to recover the price from B (i).

Notice that the rule applies only where a contrary intention does not appear from the terms of the contract or otherwise. It has been held in this connection that there is no implied condition as to title, where goods

(f) *Martindale v. Smith*, 1 Q.B. 389.
(g) *Aron & Co. v. Comptoir Wagemont* (1921), 3 K.B. 435.

(h) *Baldeodas v. Howe*, 6 Cal. 64.
(i) *Rowland v. Dival* (1923), 2 K.B. 500.

are sold in execution of a decree or when they are sold by an auctioneer (j) or by a pawn-broker in pursuance of his right as pledgee (k).

“Warranty” of Quiet Enjoyment

(II) Subject to the same conditions as above, there is an *implied warranty* that the buyer shall have and shall enjoy quiet possession of the goods [sec. 14, cl. (b)]. This is called a “*warranty of quiet enjoyment*”. It is an implied assurance to the buyer that he shall have the possession and enjoyment of the goods sold to him, without disturbance by the seller or any other person. Being a warranty only, its breach entitles the buyer to claim damages only from the seller therefor.

“Warranty” of Freedom from Incumbrance

(III) Subject to the conditions mentioned above, there is an *implied warranty* that the goods are free from any charge or incumbrance in favour of a third person, not declared to or known to buyer [sec. 14, cl. (c)]. This clause was invoked in a Calcutta case (l), where certain shares in a limited company were sold by the 1st defendant to the plaintiff, by delivering the relevant certificates with blank transfer forms signed by the actual registered holder of the shares. The plaintiff sold the shares to the 2nd defendants, who, however, were refused registration by the company, because, unknown to both parties, the company had a lien on the shares. On the 2nd defendants returning the shares to the plaintiff, the plaintiff sued the 1st defendant in damages. *Held*, the implied warranty of “freedom from incumbrances” was broken by the 1st defendant and the plaintiff’s claim was well founded.

“Condition” as to Description

(IV) Under sec. 15, where goods are sold by description, there is an *implied condition* that the goods shall *correspond with the description* and where good are sold by sample as well as by description, that the goods will correspond both with the sample as well as the description, correspondence with one of them being insufficient.

The sec. deals with what is called “*sale of goods by description*”. Goods are said to be sold by description when the goods being unascertained at the time of the contract, they are sought to be identified by suitable words describing their nature. Thus a contract of sale for “a Fiat Motor Car, 1954 Model” is a contract for sale of a motor car by description. The buyer in such a case relies on the description given by the seller, in agreeing to the terms of the contract. The law therefore requires the seller to deliver to the buyer in performance of the contract, an article, which answers the description given by the seller in the contract.

Description may take any form. Labels (e.g. “tiger brand paper”), numbers (e.g. 501 soap), name of the particular maker (e.g. “Eno’s Fruit Salt”), may constitute such description, if the articles are distinctively recognised by the trade or the public by such special features. Where goods are sold in accordance with specifications, the latter are held to constitute

(j) *Ex parte Villars* (1874), L.R. 9 Ch. App. 432.
(k) *Morley v. Attenborough* (1849), 3 Ex.

500.
(l) *Kissonchand v. Rampratap*, 44 Cal. W.N. 505.

description. Similarly, the date or place of shipment, may also amount to description, so that the buyer is not bound to accept goods if the seller tenders goods of another shipment in performance of the contract.

In an English case (m) "long staple Salem cotton" was agreed to be delivered but what was tendered turned out to be very good Western Madras. *Held*, that the buyer was not bound to accept the goods. Similarly, where there was a sale of certain seeds as "common English sainfoin", and there was a term in the contract that the "sellers gave no warranty as to growth, description or other matters" relating to the goods and what was delivered to the buyer was not "common English sainfoin" but "giant sainfoin", the House of Lords held that there was a breach of condition, the added terms not excluding the operation of the rule embodied in the present sec. (n). The date of arrival of contract goods at port of destination may be part of "description" of goods and may thus amount to a "condition", e.g. "afloat per S.S. 'Mortan Bay' due approximately in London on 8th June 1954." (n1). "Description" may also refer to the quality of goods, e.g. in case of foodstuffs. Where foodstuffs are purchased by description there is an implied "condition" that they are sound and of a nourishable quality (n2).

A term in a contract that the bulk is only warranted equal to sample has been held not to take the case outside the sec. (o).

Thus where "foreign refined rape oil" was sold and what was offered was rape oil mixed with hemp oil, it was held that the buyer was entitled to refuse the goods, though the goods offered tallied with the sample (o). Where a contract was for sale of certain bags of "waste silk" and samples were shown, and the goods tendered turned out to be unsaleable as "waste silk", *held*, the buyer could recover as on a breach of condition (p). Similarly, in a recent Calcutta case (q), where copper ribbon sheets used for tube wells were sold to Government, and a sample having been produced according to the specifications, the same was approved by Government expert, it was held, on the bulk not corresponding with the specifications, that the Government was entitled to refuse the goods, though the bulk agreed with the sample. This is because a sample is a test only of the quality of an article.

Notice that it is not necessary that the article offered should be perfect; what is required is that it must be saleable in the market under that description. Specific goods may also be sold by description. Notice that where goods are sold by description, the fact that the buyer has examined the goods will not prevent the sec. from applying, if the goods show a latent defect (r). It has been recently held that where goods, whether specific or unascertained, are sold under a trade description, without misrepresentation or breach of warranty, the fact that unknown to both parties, the goods of that trade description lack a particular quality, is no ground to treat the contract as a nullity, on the ground of fundamental mistake if goods supplied answer the description (s). Whether in a given case, goods are sold by description is, of course, a question of fact.

"Condition" or "Warranty" of quality or fitness

(V) As sec. 16 lays down, except as provided by the Act or any other law in force for the time being, there is *no implied warranty or condition as to quality or fitness* of the goods sold for any particular purpose.

(m) *Azemar v. Casella* (1867), L.R. 2 C.P. 431.

(n) *Wallis Sons & Wells v. Pratt & Haynes* (1911), A.C. 394.

(n1) *Macpherson Train & Co. v. Howard Ross & Co.* (1955), 2 All E.R. 445.

(n2) *In re Beharilal*, A.I.R. (1955) Mad. 71.

(o) *Nichol v. Godts* (1854), 10 Ex. 191.

(p) *Gardiner v. Grey*, 171 E.R. 46.

(q) *Kharendra v. Sec. of State*, 44 Cal. W.N. 1069.

(r) *Josling v. Kingsford*, L.R. 2 C.P. 677.

(s) *Harrison & Jones Ltd. v. Bunter, etc.* Ltd. (1953), 1 All E.R. 903.

This is a fundamental principle of the law of sale of goods, the maxim being "*caveat emptore*", i.e. "let the buyer take care". In other words, it is no part of the seller's duty in a contract of sale of goods, to give to the buyer, an article suitable for a particular purpose, or of a particular quality, unless such quality or fitness is made an express term of the contract. Thus on a sale of a penknife or a fountain pen, there is no implied term that the penknife would cut, or that the pen would write. It is the duty of the buyer alone, in all such cases, to satisfy himself before concluding the sale, that the article which he buys, is the one which he wants.

EXCEPTIONS: The rule is a strict one and hence there are exceptions to it. These are provided for by cls. 1-3 of sec. 16, as follows:

(1) Where (i) the buyer (expressly or by implication) makes known to the seller the particular purpose for which the goods are required (ii) in such a manner as to show that he relies on the seller's skill or judgment and (iii) the goods are of a description which it is the seller's business to supply, there is an *implied condition* that the goods shall be *reasonably fit for the purpose*. There is no such implied condition in such cases, however, when a specific article is sold under its patent or trade name.

For the exception to operate, all the above three conditions must be fulfilled, viz. (i) the purpose must have been disclosed; (ii) the buyer must have relied on the seller's skill or judgment; and (iii) the seller's business must be to sell such goods.

Thus where a person purchased a hot water bottle from a chemist, and the bottle burst and injured his wife, it was held that the chemist was liable in damages (t). Similarly, where any article of food, e.g. milk, is ordered from a milk dealer, there is an implied condition that the milk is fit for human consumption (u). Similarly, when a refrigerator was sold by A to B and it performed all other acts which a refrigerator usually does but failed to make Ice, *held*, this amounted to a breach of an implied condition (v). It has been recently held in England that on a sale of a hair dye, there is an implied warranty that it was suitable for dyeing the hair of a person whose reaction to such a hairdye is normal. The warranty does not extend to protect a person of abnormal sensitivity to such a hairdye (v1). Sale of a motor car "in good running condition" makes "good running condition" a warranty (v2).

Notice that the buyer cannot be said to rely on the seller's judgment or skill, when he selects the article himself after inspection. On the other hand, where he does rely on his skill, the fact that the buyer could have discovered the defect by use of ordinary diligence affords no defence. The seller must also be selling the goods in the ordinary course of his business. If the seller does not generally deal in the goods sold, the exception will not apply. It makes no difference, whether the seller is a manufacturer or a mere dealer of the goods in question.

Notice also that as the proviso to cl. 1 provides, this exception does not apply, where the specific goods are sold under their patent, or trade name.

Thus when a patent smoke consuming furnace was ordered by the plaintiff by its patent name for his brewery and the same being forwarded to him, proved useless, *held*, he had no cause of action against the defendant (w). Similarly, where a Fiat car of a

(t) Priest v. Last (1903), 2 K.B. 148.

(u) Frost v. Aylesbury Dairy Co. (1905), 1 K.B. 608.

(v) Evans v. Stella Benjamin, A.I.R. 1951 Cal. 470.

(v1) Ingham v. Emcs (1955), 2 All E.R. 740.

(v2) Kanak Kumari v. Chandanlal, A.I.R. (1955) Pat. 215.

(w) Chanter v. Hopkins (1838), M. & W. 399.

particular model is ordered, the seller does all he is liable for, by forwarding the said model to the purchaser. Notice however that a sale of a Fiat car is different from a sale of a car made by the Fiat Company (x).

(2) The second exception to the above rule is made by cl. 2 of sec. 16, under which where goods (i) are bought by description (ii) from a seller who deals in such goods, there is an *implied condition* that (iii) the goods shall be of a "merchantable quality". (iv) Where, however, the buyer has examined the goods, there is no such warranty, as regards defects which such examination ought to have revealed (i.e. as regards patent defects). The implied condition as to "merchantable quality" arises only if the first two conditions are both fulfilled.

What is "*merchantable quality*" has never been properly defined. The nearest description of the term is that the article "must be saleable in the market under the denomination mentioned" (y). In other words, in order to be "merchantable" the article must be of such quality, and in such condition, that reasonable men would accept the article as performance of a promise (z). It thus includes quality, condition, label, etc.

Thus where there was a sale of Manilla hemp and the hemp tendered, though Manilla hemp, was so damaged by sea water that no one in the market would accept it as Manilla hemp, it was held that the above condition was broken (a). Similarly, where a person bought a bottle of Stone's Ginger wine from a dealer and the bottle broke at the neck, when being opened, it was held that the seller was liable as on breach of the above condition (b). In a Privy Council case, a purchaser of a woollen garment from a retailer, who developed "dermatitis" by wearing the same, was held entitled to recover damages against the retailer, as though the garment looked alright on the outside, there was excess of sulphites left therein, during manufacture, which no inspection could have revealed. The Privy Council said: whatever the meaning of "merchantable" may be, it does mean that an article sold, "if only meant for one's use in the ordinary course, is fit for that use" (c). In a recent English case a dealer supplied a quantity of coal, described as "Coalite" to a housewife in pursuance of her order. The fuel contained explosive matter, which on exploding caused damage. *Held*, the goods were "unmerchantable" owing to the presence of the explosive substance and therefore the dealer was liable (d). On the sale of a secondhand crushing machine by description after inspection, it was found to be of an unmerchantable quality by reason of a latent defect. *Held*, inspection did not deprive the buyer of the right to reject the goods, as the defect could not be discovered by mere inspection (d1).

Notice that as the proviso says, there is no such implied condition where the buyer examines the goods, so far as patent or obvious defects are concerned. Of course, for latent defects, which no examination could reveal, the implied condition subsists.

In a Madras case certain skins "of fair average quality" were sold. The skins were to be inspected and approved by certain specialists in skins. After such inspection and approval, the skins were sent to England, where on being processed, certain defects were found therein, which were not visible in their dry condition; *held*, the defects being latent, the buyers were entitled to recover as on a breach of condition, but having accepted the skins, they could only counterclaim for damages, against the seller's claim for the price (e).

(x) Bristol Tramways v. Fiat Motors (1910), 2 K.B. 831.

(y) Gardner v. Grey (1814), 4 Cowp. 144.

(z) Bristol Tramways v. Fiat Motors, *Supra*.

(a) Jones v. Just (1868), L.R. 3 Q.B. 192.

(b) Morelli v. Fitch (1928), 2 K.B. 636.

(c) Grant v. Australian Knitting Mills (1936), A.C. 85.

(d) Wilson v. Ricket Cockerill & Co. (1954), 1 All E.R. 868.

(d1) Hussainbhai v. New India Corp., A.I.R. (1955) Mad. 435.

(e) Khoyee & Co. v. Gordon Woodroff & Co. (1937), Mad. 497.

(3) Notice that a condition as to fitness for a particular purpose or as to quality, may also arise on account of a custom of trade (cl. 3). Notice further that an express condition or warranty does not negative a condition or warranty implied by the Act, unless inconsistent with it (cl. 4).

Sale by sample

(VI) Under sec. 17 on a *sale by sample*, the implied conditions are (i) that the bulk shall correspond with the sample as regards quality; (ii) that the buyer shall have reasonable opportunity of comparing the bulk with the sample; and (iii) that the goods shall be free from any defect which renders them "unmerchantable" and which would not be apparent on a reasonable examination of the sample.

A sale is by sample where there is a term in the contract, express or implied, to that effect. The effect of the sec. is that where goods are sold by sample, there should not be latent defects therein which renders them "unmerchantable". Further, they must conform to the quality of the sample. This is so, even if the goods are sold "subject to all faults" (f). Notice that delivery of goods by the seller to a person named by the buyer operates to terminate the buyer's right to reject the goods as not being according to sample (g).

Warranty on hire-purchase: Notice that it has been recently held in England that where as a result of a warranty of fitness, a person is induced to enter into a hire purchase agreement with a third person with regard to an article, e.g. a motor car, he is entitled to damages for breach of such express warranty, though the transaction was not one of sale (h).

"**Warranty of performance**" means that a particular article of sale, e.g. a machine, will be capable of producing certain results. When such warranty is broken, the purchasers can, it has been held recently, claim as damages, either the capital cost incurred, less anything obtained by disposing off the material or on the basis of profit lost on account of the machine falling short of its warranted performance (i).

Implied Terms: The Court should not imply a term in a contract because it would be a reasonable term to include, if the parties had thought of the matter or because one party, if he had thought about the contract, would not have entered into it unless the term was included. It must be such a term that both parties must have intended that it should be a term of the contract and have only not expressed it because its necessity was so obvious that it was taken for granted (j). It has been held in England that the Court would read an implied term into a contract only where it is clear that both parties intended that term to operate as a part of the contract (k). Where therefore there was an unqualified contract between Indian sellers and British buyers for certain quantity of jute and the contract was not expressed to be "subject to quota", held, on the quota system being introduced into India during the relevant period, that the sellers could not claim to

(f) *Champanhae & Co. v. Waller & Co.* (1948), 2 A.E.R. 724.

(g) *Ruben Ltd. v. Faire Bros.* (1948), W.N. 507.

(h) *Brown v. Sheen & Richmond Car Sales Ltd.* (1950), All E.R. 1102, followed *Shanklin Pier Ltd. v. Detil Products* (1951),

2 All E.R. 471.

(i) *Cullinane v. Br. "Rema" Mfg. Co.* (1953), 2 All E.R. 1257.

(j) *Comptoir Commercial v. Power Son & Co.* (1920), 1 K.B. 868.

(k) *Ralli Bros. v. Compania Naviera, etc.* (1920), 2 K.B. 287.

imply the said term into the contract, although both parties knew that the contracts could only be met out of the seller's quota as allowed to him (l).

Government Controls: In cases where, after a contract of sale has been entered into, the commodity becomes subject to Government control, so as to be saleable or importable only under a Government licence, it is a question of fact depending on the terms of the contract and facts of each case as to which party is bound to procure such licence. Sometimes the duty may be cast on the seller, sometimes by the terms of the contract or otherwise, the duty may be cast on the buyer (m).

PASSING OF PROPERTY

Rules as regards passing of property (secs. 18-26): Secs. 18-26 deal with the important question of "passing of property". "Passing of property" means passing of ownership and the question considered here is: on a contract for sale of goods, when does the subject-matter of sale cease to be of the ownership of the seller and vest in the purchaser as owner thereof? The question is important from many points of view. If property has passed to the buyer, the risk of destruction or deterioration of the goods sold, falls on the buyer, and not on the seller, though the goods may be still in the seller's possession (sec. 26 seq.). A creditor of the seller also, cannot attach the goods in execution of a decree against the seller. Further, if the seller becomes insolvent before giving delivery of the goods to the purchaser, the Official Assignee of the seller can have no claim against the goods as property in them has already passed to the purchaser.

When property passes

Certain rules are laid down by the Act, for determining when property passes on a contract for sale of goods. These are as follows:

(I) Where a contract is for unascertained goods, no property in the goods is transferred to the buyer unless and until the goods are ascertained (sec. 28). This is a fundamental rule and it applies, irrespective of what the parties intended. Thus a "sale" of 100 maunds of rice from a granary containing a larger quantity, has not the effect of transferring property in the 100 maunds to the purchaser. It amounts only to an agreement of sale. It is only when the 100 maunds are separated from the bulk by the seller and appropriated by him to the contract with the assent of the purchaser, that property will pass from the seller to the buyer. Notice that in such a case, the fact that a delivery order has been issued or that the goods are entered in the buyer's name in the books of the warehouse-keeper makes no difference.

(II) If goods are ascertained, the second rule with regard to passing of property is laid down by sec. 19: Where there is a contract for the sale of specific or ascertained goods, the property in them is transferred to the buyer *at such time, as the parties intend it to be transferred*. In other words, where once the goods which are the subject-matter of a sale are ascertained, it is purely a question of the intention of the parties, as to when property is to pass. If the parties so intend, it may pass immediately on the making of the contract, although the price has not been paid and

(l) Partamball v. K. C. Sethia Ltd. (1951),
* All E.R. 352.

(m) See Taylor v. Landour & Co. (1940),
4 All E.R. 335.

delivery has yet to be given. It may, if so intended, pass only with the payment of the price or giving of delivery or both. The whole question being thus entirely dependent on the intention of the parties, sec. 19, cl. (2), lays down how such intention has to be gathered. According to the clause, in ascertaining the intention of the parties, regard is to be had to the terms of the contract, to the conduct of the parties, and to the circumstances of the case. On the construction of the above materials, the parties' intention as regards passing of property is to be deduced, and effect is to be given to whatever may be the intention, as so deduced. This is another fundamental rule.

(III) It may happen, however, that intention of the parties cannot be deduced as suggested above or they may not have determined amongst themselves as to when property is to pass. In such cases, the Act lays down a series of rules in secs. 20-24 in accordance with which the intention of the parties will be ascertained in a given case. Notice clearly that these rules apply only if a different intention does not appear (sec. 19, cl. 3). These rules are as follows :

How Intention Ascertained

(a) Where there is an *unconditional contract* for the sale of *specific goods*, in a *deliverable state*, the property in the goods passes to the buyer when the contract is made and it is immaterial that the time for payment of price or delivery of goods or both is postponed (sec. 20).

Thus where A agreed to sell B a standing stack of hay for a fixed price, payable on the 4th of February next and by the contract the stack was allowed to remain on the premises till the 1st of May following, it was held to be an immediate sale, the property in the stack passing to B immediately the contract was made (n). Notice in this connection that, as recently held by the Bombay High Court (o), endorsing a railway receipt in favour of another, does not, by itself, pass property in the goods to the endorsee. It merely constitutes the endorsee, the agent of the consignor, to receive the goods. Such an endorsement, by itself, does not constitute the endorsee either a *bona fide* pledgee or transferee for value of the goods represented by the railway receipt.

(b) Where there is a contract for sale of *specific goods* and the *seller is bound to do something to the goods* for the purpose of putting them in a deliverable state, the property does not pass till such thing is done and the buyer has notice thereof (sec. 21).

Thus where a condensing engine which was fixed at a particular place was agreed to be sold F.O.R. for a fixed price and the engine was damaged while being taken to the Railway, it was held that the property had not passed to the buyer, as the seller had, under the contract, to sever the engine and place it on rail before it could be said to be in a deliverable state (p).

(c) Where there is a contract for the sale of *specific goods* in a *deliverable state* but the *seller is bound to weigh, measure, test or do some other thing with reference to them*, for ascertaining the price, the property does not pass till such act or thing is done and the buyer has notice of it (sec. 22). Notice that the sec. applies only where, by contract, the seller has to do something mentioned therein.

Thus where a certain quantity of starch was sold at £— per cwt. and the seller, having directed his warehouseman to weigh and deliver the same to the purchaser,

(n) Tarling v. Baxter (1827), 6 B. & C.

360.

(o) Shamji v. N.W. Rly., 48 Bom. L.R.

698.

(p) Underwood v. Burgh Castle Syndicate (1922), 1 K.B. 343.

became bankrupt, after part of it was weighed and delivered over to the buyer, it was held, on a contest between the Official Assignee and the purchaser, that weighing by the seller being a condition precedent of the passing of property, the balance of the goods remained the property of the seller and had not become the property of the buyer (q).

If the weighing, etc. has to be done by the buyer for his own satisfaction, the sec. does not apply (r).

Where a heap of clay was sold at a certain price per ton and the buyer was to load it in his carts and weigh each load on his way to the destination, held, the property passed as soon as the contract was made as it was for the buyer's convenience that weightment was to be made and not for that of the seller's (s).

(d) Where there is a contract for the *sale of unascertained or future goods by description* and goods of that description and in a deliverable state are unconditionally appropriated to the contract by the seller with the assent of the buyer or by the buyer with the assent of the seller, the property in the goods thereon passes to the buyer. Such assent may be given expressly or impliedly and either before or after the appropriation (sec. 23). The sec. refers to unascertained or future goods sold by description, e.g. 100 bales of Broach cotton, 1st quality, for April-May "vaida"; in such a case, for property to pass, the following conditions will have to be fulfilled: (i) goods of the contract description must be produced or obtained; (ii) they must be in a deliverable state; (iii) they must be appropriated, i.e. allocated to the contract; (iv) the appropriation must be unconditional; and (v) it must be with the consent of both the parties. On such appropriation, property in the bales will pass from the seller to the purchaser.

Notice that the goods must be of the *contract description*. Thus if 10 hogs-head of claret are sold, sending 15 hogs-head will not accord with the contract description (t). The goods must also be in a *deliverable state*, e.g. if the wine is to be packed and labelled by the seller in a certain way, the seller must have done so, before the sec. can apply. Further, the goods must have been *unconditionally appropriated* by the seller to the contract.

As regards unconditional appropriation, cl. 2 of sec. 23 provides that where the seller delivers the goods to the buyer or to a carrier or other bailee for transmission to the buyer, he is deemed to have unconditionally appropriated the goods to the contract, unless he has reserved the right of disposal to himself. How this can be done is explained by sec. 25. In other words, if the appropriation is conditional, i.e. if goods are tendered by the seller to the buyer with a stipulation that delivery is only against payment in cash, no property will pass till cash payment is made. Notice that under cl. 2, delivery to a carrier amounts in law to an unconditional appropriation of the goods to the contract. In other words, a common carrier, under this cl., is an agent of the buyer, not only for receiving the goods, but also to assent to their appropriation on behalf of the buyer, unless the "*Jus desponende*" is reserved by the seller (u). The seller may by suitable devices (see sec. 25 seq.), retain the "*jus desponende*", i.e. "the right of disposal" to himself. In such cases, delivery to carrier will not amount to unconditional appropriation.

(q) *Hanson v. Meyer* (1805), 6 East. 614.

(r) *Turley v. Bates* (1863), H. & C. 200;

Hoe Kim v. Howing, 37 Bom. L.R. 866.

(s) *Turley v. Bates* (supra).

(t) *Cuncliff v. Harrison* (1851), 6 Ex. 903.

(u) *Colonial Ins. Co. v. Adelaide Ins. Co.*,
12 A.C. 128.

Lastly, the appropriation must be *assented to by both the parties*, either before or after the event.

Thus in *Aldridge v. Johnson* (v) A agreed to buy 100 quarters of barley from K out of a large bulk, which A had inspected. Under the contract A was to send his own sacks which K was to fill up and put on rail, free of charge. 200 sacks having been sent by A, K filled 155, but being on the eve of bankruptcy, he emptied them out again. *Held*, the property in the 155 sacks had passed to A, as A had, by sending his own sacks, assented in advance to the appropriation of goods by K to the contract. Similarly, where A in England ordered from B at Basle in Switzerland a parcel of dyes to be sent by post, *held*, on posting the parcel at Basle, property passed to the purchaser (w).

The buyer's assent may be subsequent also (x).

Thus where A bought 20 hogs-head of sugar from B out of a large lot and out of these, 4 hogs-head were filled and delivered and as regards the remaining 16, they were filled up and appropriated by the seller and the buyer, being thereafter informed of the fact, replied that he would take them away later, *held*, the property had passed to the buyer on the appropriation being subsequently assented to by him (x).

"Shares" are goods under the Sale of Goods Act. Accordingly, where a contract for the sale of shares of any particular company is made generally, without specification of their serial numbers, the sale becomes complete upon delivery to the purchaser of the share certificates and relevant transfer forms signed by the registered holder and the purchaser on his part accepting the same and paying for them (y).

Notice that appropriation of wrong goods to the contract is no appropriation. Further, it is open to the parties by an express agreement to agree that the property shall pass even before the goods are completely manufactured and appropriated to the contract. This is because all the above rules are subject to a contrary intention not appearing on the contract.

(e) Where goods are delivered to the buyer "on approval" or on "sale or return" or similar terms, the property passes to the buyer, (i) when he signifies his approval or acceptance or (ii) does any other act adopting the transaction or (iii) if, without signifying his approval or acceptance, the buyer retains the goods without notice of rejection, then, if time is fixed for the return of the goods on the expiry of the time and if no time is fixed, on the expiration of a reasonable time (sec. 24).

A contract on the basis of "sale or return" does not pass property to the buyer at once. Property passes when the buyer exercises his option to buy. This he can do in a variety of ways as set out in the sec. The transaction is adopted when the buyer does any act of dominion over the goods showing an unequivocal intention to buy, e.g. if he pledges the goods with a third party. Failure or inability to return the goods to the seller does not necessarily imply an election to buy, e.g. where a horse delivered to the purchaser on the above basis died while in his custody without any fault on his part, it was held that no property had passed to the purchaser (z). Goods delivered to the buyer on what is called "*jangad*" terms are within the sec. (a). "*Jangad*" means giving delivery of goods to a prospective

(v) (1857), 26 L.J.Q.B. 296.

(w) *Badische Aniline v. Basle Chemical Works* (1898), A.C. 200.

(x) *Rhodes v. Thwaites* (1827), 6 B. & C. 388.

(y) *Bharucha v. Wadilal*, 28 Bom. L.R. 777 (P.C.).

(z) *Elphic v. Barnes* (1880), 5 C.P.D. 321.

(a) *Durgabai v. Saraswatibai*, 31 Bom. L.R. 411.

purchaser for inspection and buying, if approved. Of course, if the parties have made an express stipulation as to when the property is to pass, the sec. will not apply and the case will be governed by the special agreement (b).

In a recent English case certain motor vehicles were sold at an auction to a person who was the highest bidder. During the sale the purchaser made certain misrepresentations as to his identity to the auctioneer. Believing them the auctioneer allowed the purchaser to take delivery of the vehicles and accepted in payment a cheque, accompanied with the purchaser's certificate that the property was not to pass till the cheque was honoured. The purchaser sold one vehicle to a third person who sold it to the defendant. The cheque was dishonoured. On the auctioneer bringing a suit against the defendant to recover the vehicle, *held*, (1) this was not a case of larceny by trick so as to prevent property from passing to the purchaser; (2) that property passed on the fall of the hammer and that there was no effective condition that it should not pass till the cheque was honoured; (3) that property having so passed, the certificate of the purchaser had not the effect of re-vesting the property in the auctioneer (c).

Reservation of right of disposal (sec. 25)

The above rules with regard to passing of property are subject to the important qualification that in all cases of sale of goods, whether the goods are specific, unascertained or future goods, the seller may, by the terms of the contract or appropriation, reserve the right of disposal of the goods to himself till certain conditions are fulfilled. In such cases, notwithstanding delivery of goods to the buyer or to the carrier or other bailee for the purpose of transmission to the buyer, property will not pass till the conditions are fulfilled.

Two cases are enumerated by cls. (2) and (3) of sec. 25 in which the seller is deemed to have reserved the right of disposal to himself: (i) where goods are shipped by sea and by the bill of lading the goods are made deliverable to the order of the seller or his agent and (ii) when the seller draws on the buyer for the price and sends the bill of exchange and the bill of lading to the buyer together, to secure acceptance or payment of the bill. In such a case, no property passes to the buyer till he accepts or pays the bill of exchange (c1). His retention of the bill of lading will not pass the property to him. To these, a third case may be added: (iii) where a seller makes out the bill of lading in the name of himself or his order and forwards the documents endorsed in blank to his bankers to be delivered to the purchaser either on D/A (documents against acceptance) or D/P (documents against payment) terms: in either of these cases, no property will pass to the purchaser till the conditions on which the appropriation is made are satisfied by him.

Notice that sending a bill of lading, with advice only of the bill of exchange, will not call this sec. into operation. Notice further that endorsing a railway receipt in favour of another, does not of itself pass property in the goods to the endorsee. It merely constitutes the endorsee, the agent of the endorser to receive the goods (d).

In a Bombay case, the plaintiffs having appointed defendants as their agents for sale of their cars, sent 20 cars to the defendants at Ambala, the consignment being at the owner's (plaintiffs) risk. The railway receipts were made out in the name of the plaintiffs as consignees and were endorsed by them in blank. The plaintiffs sent the

(b) *Manders v. Williams* (1849), 4 Ex.

339.

(c) *Dennant v. Skinner* (1948), 2 K.B.

164.

(c1) *State of Madras v. Ramlingam & Co.* (1956), 2 Mad. L.J. 384.

(d) *Shamji v. N.W. Rly.*, 48 Bom. L.R. 698.

receipts through their bankers along with a bill for the price of the cars to be recovered from the defendants against the railway receipts. The consignment, however, was destroyed by fire in transit. The defendants having refused to pay the bill, the plaintiffs sued to recover the amounts; *held*, the appropriation by the plaintiffs was not absolute and final, because it was conditional on payment by the defendants of the plaintiffs' bill, the property therefore did not pass to the defendants and the defendants therefore were not liable for the price (e). In another case, a cargo of umber was shipped on board a ship chartered by the buyers. The sellers took out bills of lading making cargo deliverable to order or assigns. They also drew a bill of exchange on the buyer for the price which they discounted with a bank handing over to the latter the bill of lading to be given up to the buyer on acceptance and payment of the bill. The buyer first refused to accept the bill but subsequently tendered the amount to the bank which however refused to accept the tender and sold off the cargo, *held*, on tender of price by the buyer the property in the cargo passed to him and the sale by the bank therefore was wrongful (f).

Passing of risk (sec. 26)

Under sec. 26, unless otherwise agreed, the goods remain at the seller's risk till property has passed to the buyer. After that event, they are at the buyer's risk, whether delivery has been made or not.

The rule is subject to two qualifications: (i) if delivery has been delayed by the fault of the seller or the buyer, the goods are at the risk of the party in default, as regards loss which might not have arisen but for such default. (ii) The rule laid down by the sec. does not affect the rights and liabilities of the seller or the buyer as bailee of goods for the other.

Generally, "risk", i.e. the "liability to bear the loss if the property is destroyed or deteriorates", passes with "property", but this is subject to the agreement between the parties. Thus parties may, by special agreement, stipulate that "risk" will pass some time after or before the "property" has passed. Thus in case of C.I.F. contracts (see seq.), the "risk" *prima facie* passes to the buyer on the goods being shipped. In an F.O.B. contract (see seq.), the goods are *prima facie* at the seller's risk till he puts them on board. Where a motor car was garaged for sale at the customer's risk, the garage keeper was held not liable for loss of the car caused by his servant (g). Even unascertained goods may be at the buyer's risk, if the parties so agree. Where price is payable, by agreement, only on the safe arrival of the goods, the goods are at the seller's risk, till they arrive safely at their destination (h).

TRANSFER OF TITLE

Passing of property and passing of title distinguished

Secs. 18 to 26 deal with the question when property in any particular subject of sale passes from the seller to the buyer. As explained before, this refers to the transfer of ownership of goods from the seller to the buyer and the conditions under which such transfer takes place. It is throughout presumed that the seller is a *full owner* of the goods, so that on transfer of property in the goods, the buyer also becomes the full owner. But supposing that owing to certain facts, the seller is not the full owner, but a *qualified*

(e) *Ford Automobiles v. Delhi Motor Co.*, 24 Bom. L.R. 440.

(f) *Maritoba v. Imperial Ottoman Bank* (1874), 3 Ex. Div. 164.

(g) *Waneka v. Wingrien* (1889), 58 S.J. Q.B. 519.

(h) *Calcutta Co. v. De Mettos* (1863), 32 L.J.Q.B. 323.

owner of the goods, e.g. as being an agent of the true owner or a pledgee from the true owner, or even a thief, who has stolen the goods from the true owner, the question that naturally arises is whether on a transfer of property from such a qualified owner to another, the latter, i.e. the transferee, becomes a qualified owner also or a full owner and if so under what conditions. In other words, what is the *title* which the transferee gets when he obtains a transfer of property in goods from a qualified owner to himself? This question is considered by secs. 27 to 30 which deal with what is called a "transfer of title".

General rule (sec. 27)

The general rule as regards transfer of title on a sale of goods is that expressed by the maxim "*nemo dat quod non habet*", which means, that "no seller can give to the buyer a better title than what he himself has". If the seller, therefore, has no title, or a defective title, the buyer's title will be equally wanting or defective as the case may be, though he may have purchased the goods *bona fide* and for value.

This rule is embodied in cl. (i) of sec. 27 which says that "subject to the provisions of the Act and of any other law at the time in force, where goods are sold by a person, who is not the owner thereof and who does not sell under the authority or with the consent of the owner, the buyer acquires no better title to the goods than the seller had, unless the owner is precluded by his conduct from denying the seller's authority to sell".

Thus where A having sold goods to B, assigned the bill of lading with regard thereto to another, who *bona fide* paid full price therefor to A, *held*, the assignee from A obtained no title to the goods as A had none to give (i). Similarly, where A finds a ring belonging to another and thereafter sells it to a third person who purchases it for value and without notice that A is not the owner, the true owner can recover it from the person, for A having no title could pass none to the latter (j).

Exceptions to the rule

To the above rule, however, which obviously works very hard against innocent transferees, there are several exceptions. They are laid down by secs. 27-30, and are as follows:

(I) Where goods are sold by a person *with the authority* or with the consent of the owner, e.g. as agent (sec. 27, cl. 1), the transferee gets a good title.

(II) Where the true owner is *estopped* by conduct from denying the seller's authority to sell (sec. 27, cl. 1), the transferee will get a good title as against the true owner.

Thus where the true owner of certain machinery in the possession of another, knowingly allowed it to be attached in execution as that other's property and did not lodge any claim thereto for some months and the machinery was thereupon sold by the creditor in execution of his decree, *held*, the true owner was estopped from denying the title of the person in whose possession the machinery had remained (k).

(i) *Ogle v. Atkinson*, 5 Taunt. 759.

(j) *Faruquaharson v. King* (1902), A.C.

325.

(k) *Pickard v. Sears* (1837), 6 A. & E. 469.

Notice, however, that before a good title by estoppel can be made, it must be shown that the true owner had actively suggested or held out the other person in question as the true owner or as a person authorised to sell the goods. In a recent English case (l), the owner of certain timber lying at the docks, had authorised the dock company to deliver the same on delivery orders signed on his behalf by C. C fraudulently signed delivery orders requesting the dock company to transfer the timber to the order of Mr. Brown, a fictitious person. The company did so and as Brown, C endorsed the orders to the defendants, who *bona fide* paid value therefor. In an action by the true owner against the defendants, *held*, by the House of Lords, that there was no estoppel against the true owner, who had himself done nothing actively to mislead the defendants and that, therefore, no title passed to the defendants in respect of the goods, they purported to purchase.

(III) The third exception is with regard to a "*mercantile agent*". Sec. 27, proviso, lays down that where a "*mercantile agent*" is (i) with the consent of the owner, (ii) in possession of goods or any documents of title to goods, (iii) any sale made by him, (iv) while acting in the ordinary course of business as a mercantile agent, shall be binding on the true owner if (v) the buyer has acted in good faith and (vi) has not, at the time of contract, notice that the seller had no authority to sell.

Notice that all the above six conditions must be satisfied, before this exception can apply. Notice further that it applies only in case of a mercantile agent (see ante) and not of any agent. Thus factors, auctioneers, brokers, etc. are mercantile agents but a warehouse-keeper is not, nor is an ordinary agent to canvass orders. Similarly, he must have obtained possession of the goods with the consent of the true owner. Notice in this connection, that fraudulent intention on the part of the mercantile agent will not take the case out of the sec. if he has obtained possession of the goods from the owners with his consent.

Thus where a mercantile agent obtained some diamonds from the true owner falsely pretending that he had a customer who wanted to purchase them and he afterwards fraudulently pledged the goods to secure an advance for himself, *held*, the owner was bound by the transaction of pledge (m).

The mercantile agent must also have sold the goods in his ordinary course of business. Thus where a registered owner of shares handed over the share certificates with blank transfer forms duly signed by the shareholder to a certified share broker for sale, and the broker having sold the shares to an innocent purchaser, absconded with the proceeds, it was held that the purchaser had acquired a good title against the true owner under the principle of the above exception (n). Similarly, where a motor car agent for sale sold the car at a price below that authorised by the owner and misappropriated the proceeds, it was held that the innocent purchaser had obtained a good title against the true owner (o).

The same rules apply where documents of title are disposed of by the above persons. The principle of the exception applies to a fraudulent pledge as well as a fraudulent sale (see sec. 178, Contract Act). Goods entrusted

(l) *Faruquaharson v. King* (supra).

(m) *Oppenheimer v. Attenborough* (1908),
1 K.B. 221.

(n) *Fazal v. Mangaldas*, 23 Bom. L.R.
1144.

(o) *Folkes v. King* (1923), 1 K.B. 282.

to a broker, who is not a "mercantile agent" on "jangad" terms are not protected by sec. 27 (p).

(IV) Where one of *several joint owners* of goods has the sole possession thereof, with the consent of the others, any purchaser from such person, for value without notice, at the time, of the seller's want of authority to sell, acquires a good title thereto against the other joint owners (sec. 28).

Thus if two persons are joint owners of a horse, which is kept by one of them by consent, a fraudulent sale by such person as full owner to an innocent purchaser, would be binding on the other joint owner.

(V) Where the seller has obtained possession of the goods under a *contract voidable* under secs. 19 and 19A of the Contract Act, any sale by such person, before the contract is rescinded, to another, who buys for value without notice of the seller's defect of title, gives a good title to such purchaser as against the true owner (sec. 29).

Secs. 19 and 19A of the Contract Act refer to contracts which are voidable on the ground of coercion, undue influence, fraud and misrepresentation. If before a contract is avoided by the party entitled to do so, on any of the above grounds, the other party effects a sale of the goods in favour of an innocent purchaser the latter acquires a good title as against the true owner.

In a recent English case X offered to buy a "Standard" car from the defendants for a certain price and in order to obtain immediate possession of the car, which he said, he wanted to sell to a customer, paid £10 down, gave a cheque for the balance and left his own "Hillman" car as security; the agreement being that X should not sell the "Standard" till the cheque was cleared. X subsequently removed the "Hillman" from the defendants without their consent and sold the "Standard" to the plaintiffs, who purchased the same in good faith and for value without notice of defect in X's title. Later, X having been prosecuted for cheating, *held*, in a suit between the plaintiffs, purchasers and the defendants, that the plaintiffs were entitled to the "Standard" because X had obtained the car with the consent of the owners and therefore could pass a good title (q).

Notice that the case of mutual mistake is not within the sec. nor the case where there is no contract at all for want of *assensus ad idem*.

As was recently observed by the Supreme Court, where possession of goods is obtained by fraud or misrepresentation, the contract would only be voidable but not void. Where however the fraud is such that there has been no *assensus ad idem*, e.g. if fraud has induced an error as to the identity of the person, the contract is void and no title can pass. The question of criminal liability in such a case is irrelevant (r).

(VI) Where a *person having sold goods*, continues in possession thereof or of documents of title to the goods, the delivery or transfer by such person or by a mercantile agent acting for such person, of the same, by way of sale, pledge or other disposition, will pass a good title to the transferee, if such latter person has acted in good faith and without notice of the previous sale (sec. 30, cl. 1). Notice that two conditions must be fulfilled before the sec. can apply: (i) the seller must be in possession of the goods as seller and not in any other capacity. Thus where on a sale being com-

(p) *Amratlal v. Bhagwandas*, 41 Bom. L.R. 609.

(q) *Du Jardin v. Beadman Bros.* (1952), 2

All E.R. 160.

(r) *Central National Bank v. United Industrial Bank* (1954), S.C.J. 54.

pleted the buyer asks the seller to keep the goods as his bailee, the sec. will not apply. Similarly, the seller in possession as seller must have parted with that possession in favour of the *bona fide* transferee.

Thus where A purchased certain casks of wine from B which were warehoused with C and B afterwards obtained advances from C (who acted *bona fide*) on the security of the same casks, *held*, in a contest between A and C on B's insolvency, that A was entitled to the goods because there had been no fresh delivery by B to C after the pledge (s).

(VII) Similarly, where a person having bought or agreed to buy goods, obtains, with the consent of the seller, possession of the goods or of the documents of title to the goods, the delivery or transfer by such person or by a mercantile agent acting for such person, of the goods or documents, by way of sale, pledge, or other disposition thereof, will be valid and effective, if the person receiving the same, acted *bona fide* and without notice of the seller's lien (if any) (sec. 30, cl. 2).

The last two cases deal with the fraudulent disposition of goods sold, by either the seller or by the buyer, while they are in respective possession of the goods in question. If the conditions of the two clauses are satisfied, the *bona fide* transferee for value gets a good title to the goods, though the actual seller had no title or only a defective title.

Thus where a seller of goods sent to the buyer a bill of lading accompanied by a draft to be accepted by the buyer for the price of the goods, and the buyer having obtained the bill of lading endorsed it to another who took it without notice of any objection to the buyer's title, *held*, on the buyer subsequently becoming insolvent without payment of price, that the transfer by the buyer of the bill of lading to the sub-purchaser was effective against the true owner and the latter therefore could not stop the goods in transit (t).

Notice that a person in possession of goods under a "hire purchase" agreement, which gives him only an option to buy, is not within the sec. (u). If the agreement of "hire purchase" amounts to a "sale" the sec. would apply (v).

(VIII) The opening words of sec. 27 make the general rule as regards passing of title, "subject to provisions of the Act and of any other law for the time being in force". Under such other laws, a transferor is, in some cases, able to pass a better title to the transferee, than what he himself has. Thus, under the Civil Procedure Code, a Receiver can pass good title to the property he sells as such receiver though he has no title thereto. Similarly, a liquidator, an Official Assignee, a Sheriff selling property attached, can convey good title to their transferees, though they do not sell either with the consent or authority of the true owner.

In England, an important exception prevails as regards sales in "market overt", i.e. "in the open market". This is a technical phrase and means open markets held at certain places in England, by charter or custom, where things bought confer on the innocent purchaser, a complete title, though their seller's title is defective. The rule is a result of English custom and has no application at all in India.

(s) *Nicolson v. Harper* (1895), 2 Ch. 415.
(t) *Cahn v. P.B.C. Sicam Packet Co.*
(1899), 1 Q.B. 643.

(u) *Belsize Motor Co. v. Cox* (1914), 1 K.B. 224.
(v) *Cole v. Nanalal*, 49 Bom. 172.

Rules as to performance of contracts (secs. 31-44)

Secs. 31-44 lay down certain rules for the performance of contracts for the sale of goods. Most of them have already been discussed in the general law of contracts, while some require further explanation. The rules are:

(i) the seller is bound to deliver the goods and the buyer is bound to accept and pay for them, in accordance with the terms of the contract (sec. 31). Notice that under sec. 64A, if the custom and excise duty, payable on goods sold, is increased, after the making of the contract, the seller is entitled to add it to the price. Similarly, if such duty is decreased, the buyer is entitled to deduct the same from the price payable.

(ii) *Unless otherwise agreed*, delivery of the goods and payment of price are concurrent conditions (sec. 32). In other words, no delivery need be given, if the buyer is not willing to pay the price, nor need the buyer pay the price, unless the seller is ready and willing to give delivery. For the meaning of "ready and willing" see ante. No actual tender of money or goods is necessary but a capacity to do so must be proved. Notice that a wrongful repudiation of the contract by one of the parties absolves the other from the necessity of proving "readiness and willingness" (w).

The rule laid down by the sec. is subject to an agreement to the contrary. This refers to special types of contracts, known as C.I.F. contracts, C.I.F.C.I. contracts, F.O.B. and F.O.R. contracts and contracts "ex-ship". Under some of these contracts, the buyer is not entitled to demand delivery against payment of the price, while under others, the seller is not entitled to demand payment of price against an offer to deliver goods (for these contracts see seq.).

(iii) Delivery can be made by doing anything which the parties agree shall be treated as delivery and which has the effect of putting goods in the possession of the buyer or any person authorised by him (sec. 33). As noted before, delivery may be actual, constructive or symbolical. Notice that a payment of warehouse rent by the buyer to the seller does not amount to delivery to the buyer unless a part of the warehouse is actually rented (x). Similarly, the handing over of a delivery order is not delivery to the buyer unless the seller's agent holding the goods has assented thereto (y).

(iv) Delivery of part of goods sold, in process of delivering the whole, passes the property in the whole to the buyer. It is otherwise, when the part is intended to be severed from the whole (sec. 34).

Thus where goods were sold in a lot and the seller instructed the wharfinger to deliver them to the buyer who had paid for them and the buyer thereafter accepted them and took away a part, *held*, there was delivery of the whole (z).

(v) Apart from any express agreement, the seller is not bound to deliver goods, till the buyer applies for delivery (sec. 35). Notice, therefore, that it is generally the buyer's duty to demand delivery, not of the seller's to give, without a demand. Thus where the seller has agreed to deliver on board the buyer's ship, the buyer must name the ship and its readiness to load before the seller is bound to offer delivery (a).

(vi) Whether under a contract of sale, it is for the buyer to take possession of the goods or for the seller to send them to the buyer, is a question depending upon the terms of each contract. Apart from such contract, goods sold are to be delivered at the place at which they are, when the contract was made and goods agreed to be sold are to be delivered at the place where they are, at the time of agreement of sale. If they are not in existence at the time, they are to be delivered at the place where they are manufactured (sec. 36, cl. 1). Notice that where a sale is "ex-ship" the seller makes good delivery when the ship having arrived at the port of delivery the seller pays the freight and obtains a direction to the ship to deliver the goods (b).

(w) *Dayabhai v. Maneklal* (1871), Bom. H.R. 123.

(x) *Green v. Richardson* (1877), 3 App. C. 319.

(y) *MacEwan v. Smith* (1849), 2 H.L.C. 309.

(z) *Hammond v. Anderson* (1803), 1 B. & P.N.S. 69.

(a) *Armitage v. Insole* (1850), 14 Q.B. 728.

(b) *Yangtze Ins. Co. v. Lukmanjee* (1918), A.C. 585.

(vii) Where the seller is, by the contract, to send the goods and no time is fixed, he must send them within a reasonable time (sec. 36, cl. 2).

(viii) If goods are in the possession of a third person, there is no delivery by the seller to the buyer until such third person acknowledges to the buyer that he holds the goods on his behalf (sec. 36, cl. 3). This is called "attornment". This rule however does not affect the transfer of a document of title to goods, e.g. a delivery order. No "attornment" as required by cl. 3 is necessary in case of documents of title, e.g. bill of lading, in which case, delivery is made by merely endorsing the document to the buyer.

(ix) Demand and tender must be made at a reasonable hour (sec. 36, cl. 4).

(x) Unless otherwise agreed, the expenses of putting the goods in a deliverable state are to be borne by the seller (*ibid.*, cl. 5).

(xi) Where the seller delivers a lesser quantity of goods than the one contracted for, the buyer may reject the same. If he delivers a larger quantity, the buyer may accept the contract quantity and reject the rest or may reject the whole. If the goods of the contract description are mixed up with other goods, the buyer may accept the former and reject the rest or may reject the whole. In each case, the buyer is bound to pay for what he accepts. These rules, however, are subject to any usage of trade, special agreement or course of dealing between the parties (sec. 37).

Thus where coal that was delivered was partly according to contract and partly not, *held*, the buyer was entitled to reject the whole (c).

The seller may guard against an absolute assurance as regards quantity by using suitable words, e.g. "say about two tons, more or less" (d). Notice however that where the contract is to sell 200 tons "5 per cent more or less" the buyer is bound to accept delivery of 190 tons (e).

(xii) The buyer is not bound to accept delivery by instalments, unless otherwise agreed.

Thus where there was a sale of 25 tons of pepper "October-November shipment" and the seller shipped 20 tons in November and 5 tons in December, *held*, buyer could refuse to accept the whole (f).

Where a contract provides for instalment delivery, to be separately paid for, and either the seller or the buyer makes default in delivering or paying for any one or more instalments, it is a question of fact, to be determined according to the terms of the contract and the surrounding circumstances, whether the default amounts to a repudiation of the whole contract or is a severable breach, entitling the person suffering, to compensation only and no more (sec. 38). The sec. deals with what are called "*instalment delivery contracts*". Generally failure to deliver or pay for one instalment, does not amount to a repudiation or breach of the whole contract (g). The breach, however, may occur in such condition or under such circumstances as may amount to a repudiation of the whole contract (h). The question is treated by the sec. as merely a question of fact. Where a breach occurs with regard to one or more instalments of an instalment delivery contract and the breach is such that it leads to a reasonable inference that similar breaches will be committed with reference to the subsequent instalments also, the other party is entitled to treat the whole contract as repudiated (i). The tests to be applied are: (i) the quantitative ratio which the breach bears to the contract and (ii) the degree of probability or improbability that such a breach would be repeated.

Thus where 1,500 tons of meat and bone meal of a specified quality were sold, to be shipped, 125 tons monthly in equal weekly instalments and after about half the meat was delivered and paid for, the buyer found that it was not of the contract quality

(c) *Nicolson v. Bradford Union* (1866), L.R. 1 Q.B. 620.

(d) *MacConnel v. Murphy* (1873), L.R. 5 P.C. 203.

(e) *Borrowman v. Drayton* (1876), 2 Ex. D. 15.

(f) *Reuter v. Sala* (1879), 4 C.P.D. 239.

(g) *Freeth v. Burr* (1874), L.R. 9 C.P. 208.

(h) *Withers v. Raynolds* (1831), 2 B. & Ald. 882.

(i) *Millar's Karri Co. v. Waddel* (1909), 100 L.T. 128.

and therefore refused to take further deliveries, *held*, that he was entitled to do so, as the seller, under the circumstances, could not call upon the buyer to bear the risk of rejecting further deliveries of goods which did not conform to the contract (j).

(xiii) **DELIVERY TO CARRIER:** Where by the contract, the seller is bound or authorised to send the goods to the buyer, *delivery of the goods to carrier* (whether named by the buyer or not), for the purpose of transmission to the buyer or to a wharfinger for safe custody, operates in law as a delivery to the buyer. Unless the contract otherwise provides, the seller is bound to make with the carrier or wharfinger, such a contract of carriage as properly protects the buyer's interests in the goods. If he fails to do so, he is liable in damages to the buyer or the latter may refuse to treat delivery to the carrier as delivery to himself. If the route involves a sea transit and it is usual to insure the goods for such voyage, the seller shall give sufficient notice to the buyer to enable him to insure the goods. If he fails to do so, the goods shall be at the risk of the seller during such sea transit (sec. 39).

Thus where the seller delivered goods to a carrier without disclosing that they were of a value above a certain figure and as a result, the carriers were exempt from liability for loss of goods through their negligence, *held*, the seller could not recover as there had been no "delivery" (k).

The result of the sec. is to make delivery of goods to a carrier as equal to delivery to buyer. In other words, *prima facie* a carrier or wharfinger, is the buyer's agent, to take delivery of the goods. He is, however, not an agent of the buyer for accepting the goods (l). Notice that as regards insurance, the seller's duty is only to give sufficient notice to the buyer to enable him to insure the goods. The rule does not apply to "C.I.F." or "Ex-ship" contracts (m). It is doubtful whether it applies to F.O.R. contracts (m).

(xiv) Where the seller under the contract, undertakes to deliver the goods at his own risk, at a place other than where they were when sold, the buyer shall bear the risk of any natural deterioration in the goods incidental to the transit, unless otherwise agreed (sec. 40). Thus if oranges are sent by the seller at his own risk from Nagpur to Bombay, the buyer, ordinarily, bears the loss caused by the oranges becoming overripe during and on account of the railway journey. Extraordinary or unusual deterioration, however, must be borne by the seller.

(xv) Where goods are delivered to a buyer, which he has not previously examined, he is not deemed to have accepted them, unless he has reasonable opportunity of examining them and ascertaining whether they conform to the contract. The seller on a tender of goods, is bound to allow the buyer, reasonable opportunity to examine the goods for the above purpose unless otherwise agreed (sec. 41).

Thus where the seller gave notice to the buyer that the contract goods were lying at a certain wharf and were ready for delivery against payment of price and the buyers having gone to the wharf were only shown two closed casks which were said to contain the goods, *held*, no sufficient opportunity having been given to the buyers to inspect the goods, there was no valid offer of delivery by the seller (n). [Cp. sec. 38(2), Contract Act, ante.]

(xvi) The buyer is deemed to have accepted the goods when he intimates to the seller that he has accepted them or if goods having been delivered to him, he does some act with relation to them which is inconsistent with the ownership of the seller or when, after the lapse of a reasonable time, he retains the goods without intimating to the seller that he has rejected them (sec. 42). What is reasonable time is a question of fact. If time for rejection is stipulated, rejection must be within that period.

Where the buyer having seen that samples drawn from bulk were inferior to the samples originally shown to him, offered the goods for sale by auction at reduced price

(j) Robert Munro & Co. v. Meyer (1930), 2 K.B. 312.

(k) Clark v. Hutchins, 14 East. 475.

(l) Henson v. Armtage (1822), 5 B. & Ald. 557.

(m) Wimble v. Rosenberg (1913), 3 K.B. 743.

(n) Isherwood v. Whatmore, 11 M. & W. 347.

and the auction having failed to produce a purchaser, the buyer purported to reject the goods, *held*, the buyer could not do so, as he had in law "accepted" the goods (o).

(xvii) Where a buyer rightfully rejects the goods, he is not bound to return them to the seller. It is enough if he intimates his rejection to the seller (sec. 43). This means that the costs of returning goods, rightfully rejected by the buyer, must be borne by the seller.

(xviii) Where a buyer wrongfully refuses or neglects to take delivery, the seller being ready and willing and able to deliver the goods, the buyer is liable to the seller for all loss caused to him by such refusal or neglect and also for reasonable charges for the care and custody of the goods. The above rule does not affect the seller's right to treat the buyer's refusal or neglect as a repudiation of the contract (sec. 44). Notice that mere delay on the part of the buyer in taking delivery does not entitle the seller to rescind the contract, unless time is of the essence of the contract.

Notice that where no time for delivery is fixed by the contract, delivery must be made within a reasonable time. What is reasonable time, is a question of fact in each case, depending upon the nature of the commodity, the question of transport and the prevailing conditions when the contract was entered into (p).

C.I.F. Contracts

A C.I.F. contract means a contract in which the price fixed between the parties includes cost, insurance and freight. This kind of contract is fairly common in trade and has certain advantages over the ordinary kind of contract. A contract may be a C.I.F. contract in either of two ways : (i) it may be C.I.F. as to price only, i.e. it resembles the ordinary contract of sale and purchase in all respects, with this difference only, that the price includes costs, insurance and freight. This is not the real, genuine kind of a C.I.F. contract. Such a contract is governed by the ordinary rules regulating contract of the sale of goods, mentioned above, and particularly the rule that generally delivery is against payment of the price (q).

A real C.I.F. contract, however, is distinguishable from the normal contract of sale and purchase of goods in a variety of points. Its chief distinguishing feature is that, in such a contract, the seller performs his obligations under the contract, by delivering to the buyer, not the goods themselves but the relevant "shipping documents" with regard to the goods. Under such a contract, all that the buyer can demand of the seller before payment of the price is the delivery of the proper "shipping documents". The seller also cannot demand payment of the price from the buyer except on the tender of such documents to the buyer (r). The legal obligations of a seller under a proper C.I.F. contract, are : (i) to ship at the fixed port of dispatch, goods of the contract description, (ii) to procure a proper contract of affreightment for them ; (iii) to arrange for a proper insurance of the goods ; (iv) to make out a proper invoice respecting the goods ; (v) to dispatch these documents (called "shipping documents") to the buyer with all reasonable dispatch ; and (vi) to tender them to the buyer (against payment of the price) (s).

As regards (i), notice that if the goods are not of the contract description and the buyer discovers the fact after payment of price against the

(o) *Parker v. Palmer*, 4 B. & A. 387.

(p) *Dinkarra v. Sukhdai*, 48 Bom. L.R. 821.

(q) *Mohanlal v. Krishna Premji*, 30 Bom. L.R. 415.

(r) *Manbre Sacherine Co. v. Corn Products Co.* (1919), 1 K.B. 198.

(s) *Biddel Bros. v. E. Clemens Horst* (1911), 1 K.B. 214.

documents, the buyer's right to reject them is not lost (t). As to (ii), notice that the seller is bound to make out a proper bill of lading with regard to the goods and tender the same to the buyer. The bill of lading must cover the entire voyage and not a part only of it. Thus a bill of lading obtained at an intermediate port of transshipment is not sufficient to discharge the seller's obligation (u). Whether a particular document amounts to a bill of lading is a question of fact. A Mate's receipt, however, cannot be regarded as a bill of lading nor a "delivery telegram" (v). If war breaks out after shipment of goods, the buyer is not bound to accept an enemy bill of lading (w). If the buyer pays the freight, he usually takes credit for the same as against the seller. As to (iii), it is necessary that the seller should have taken out an effective policy of insurance covering the goods. The buyer is entitled to have such policy tendered to him and the fact that the goods have arrived safely is not enough. Similarly, an "open cover" policy covering all goods of the seller, or a broker's cover note or a certificate of insurance, is not enough (x). The seller is not generally bound to insure against war risk, even if war is imminent, unless there is a custom to that effect. As to (iv), an invoice may be in any form, provided it identifies the goods and makes known to the purchaser, the price he has got to pay. It need not be the invoice sent by the manufacturers (y). As to (vi), notice that all the proper "shipping documents" must be tendered to the buyer; a tender of some of them is not enough. What are proper "shipping documents" is a question of fact, depending on the custom of merchants at a particular place. A bill of lading, an insurance policy and an invoice are generally comprised in the term. A surveyor's report may also form part of them, if such a custom exists (z).

The buyer on his side, is bound to pay the price, on the proper shipping documents being tendered to him. He is bound to do so, even if the goods are destroyed, because in such a case, he has his remedy against the underwriters with whom the goods are insured or against the shipping company, under the bill of lading. It is in this sense that a C.I.F. contract has been called "sale of documents" (a). This is not strictly correct. It is rather a contract for sale of insured goods, "lost or not lost" (b). In a C.I.F. contract the purchaser cannot validly refuse to pay the price against tender of documents on the ground that the goods are not of the contract quality. In such a case he will be deemed to commit a breach of contract (c).

Notice that the above peculiarities of a C.I.F. contract have nothing to do as regards the "passing of property". This is determined by the usual legal rules (see ante) as in the case of other contracts (d). A C.I.F.C.I. contract means a contract, in which the price includes costs, insurance, freight, commission and interest. The same rules as above apply to this type of contract.

(t) *Polenghi v. Dried Milk Co.* (1914), 10 C.C. 42.

(u) *Hanson v. Hamel* (1921), 26 C.C. 232.

(v) *Steel Brothers v. Dayal*, 25 Bom. L.R. 1063.

(w) *Karberg v. Blythe* (1916), 1 K.B. 495.

(x) *Wetson v. Belgian Grain Co.* (1920), 2 K.B. 1.

(y) *Phoenix Mills v. Dinshaw & Co.*, 48

Bom. L.R. 313.

(z) *Steel Brothers v. Dayal*, supra.

(a) *Biddel's case*, supra.

(b) *Arnhold Karberg & Co. v. Blythe* (1915), 2 K.B. 379.

(c) *Gulamali v. Mahomed*, A.I.R. (1954), Mad. 268.

(d) *Bank of Morvi v. Baerlien Bros.*, 26 Bom. L.R. 155.

F.O.B. and F.O.R. Contracts

These are other special types of contracts, under which the seller undertakes to place the contract goods on board a ship or on a railway, as part of his obligations under the contract. "F.O.B." means free on board, "F.O.R." means free on rail. In case of such contracts the seller's duty ends on his delivering the goods to the proper carrier at his own expense. The goods thereafter remain at the risk of the buyer, who is responsible for the freight and other subsequent charges. The buyer, in such cases, has no right to claim delivery till the goods are actually handed over to the carrier. Delivery to carrier will then operate as delivery to the buyer, unless the seller has reserved the right of disposal of the goods to himself. Passing of property is governed by the usual rules. An F.O.R. contract does not necessarily throw on the seller the burden of procuring wagons (e).

F.A.S. Contract: Under such a contract the seller undertakes to bear the expenses of bringing the contracted goods alongside a vessel, to be procured by the buyer for carriage of the goods. The expenses of putting the goods on board the ship, is, in such cases, to be borne by the buyer.

It has been recently held by the House of Lords in England that no general rule is established for F.O.B. or F.A.S. contracts for the sale of goods, in relation to which a prohibition of export exists, that an obligation on the buyers to obtain an export licence for the goods is to be implied, in default of express stipulation between the parties. Each case depends upon the terms of the contract and the surrounding circumstances (e1).

"Ex-Ship" Contracts

These are contracts under which the seller undertakes to deliver the goods to the buyer, at the port of destination at his own expense. Under such a contract, the obligations of the seller are: (i) to deliver the goods to the buyer from a ship which has arrived at the port of delivery at a place at which goods are usually delivered there; (ii) to pay the freight and other charges, if any, to the shipowner and to relieve the goods from the shipowner's lien; and (iii) to furnish the buyer with a delivery order or some other direction to the shipowner to deliver the goods to the purchaser. The goods, in such a case, remain at the seller's risk during the voyage. The seller is bound to give sufficient notice to the buyer to enable him to insure the goods if he so desires.

Rights of unpaid seller

The unpaid seller of goods has, by law, two kinds of rights: (i) rights against the goods themselves and (ii) rights against the buyer personally. The former are treated by secs. 45-54 of the Act; the latter by secs. 55 and 56 of the Act.

Unpaid Seller: An "unpaid seller" is defined by sec. 45 as a seller (i) to whom the whole price has not been paid or tendered; (ii) and where a bill of exchange or other negotiable instrument has been accepted by him as conditional payment, when the condition has not been fulfilled by reason of the dishonour of the instrument or otherwise (sec. 45). Notice that "seller"

(e) National Coal Co. v. Girjaprasad, 86 C.L.J. 220.

(e1) Paund & Co. v. Hardy & Co. (1956) 1 All E.R. 639.

here includes persons in the position of a seller also, e.g. the agent of the seller to whom the bill of lading has been endorsed, an agent who has himself paid the price, and an agent who is personally liable for the price (f).

Unpaid seller's rights against goods (secs. 45-54)

An unpaid seller has the following rights given to him by sec. 46, as regards the goods sold. These rights are, of course, subject to the provisions of the Act and of any other law for the time being in force. Subject to the above conditions, the unpaid seller, *notwithstanding that property has passed to the buyer*, has, by implication of law,

- (i) a lien on the goods for the price thereof, while he is in possession of the goods;
- (ii) a right of stopping the goods in transit, if he has parted with the possession of the goods and if the buyer becomes an insolvent; and
- (iii) a right of re-sale, as laid down by sec. 54 of the Act. Where property has not passed, he has the same rights as above, in addition to other remedies open to him.

Unpaid seller's lien (secs. 47-49)

Under sec. 47 an unpaid seller who is in possession of the goods, is entitled to retain them in his possession, until payment or tender to him of the price, where (i) goods have been sold without any stipulation as to credit; (ii) where the goods being sold on credit, the credit has expired, and (iii) when the buyer becomes insolvent. The seller can exercise the lien, although he holds the goods as the agent or bailee for the buyer.

Notice that lien does not extend to other charges, e.g. for custody, which may be due to the seller (sec. 48).

The *lien is lost*: (i) when the seller delivers the goods to a carrier or other bailee for the purpose of transmission to the buyer, without reserving a right of disposal of the goods to himself; (ii) where the buyer or his agent lawfully obtains possession of the goods; and (iii) if the seller waives the lien. The fact that the unpaid seller has obtained a decree for the price against the purchaser, does not necessarily operate to terminate the lien (sec. 49). (iv) The lien may also be lost by estoppel, e.g. where the seller so conducts himself that he leads third parties to believe that the lien does not exist and in that belief, to act to their disadvantage (g). An unpaid seller waives his lien, when he takes a security from the buyer for the payment of the price, in place of his lien. It may also be waived if he assents to a sub-sale by the buyer.

In a Bombay case on a sale of certain shares, the relative share certificates and transfer forms duly signed were handed over by the seller to the buyer against payment of price by cheque. On the buyer subsequently becoming insolvent, *held*, by the Privy Council, that the seller had no "*Jus in re*" in respect of the share certificates or on the transfer forms, nor any lien on them, for his lien ceased when he parted with the possession (h).

Notice that as cl. (2) of the sec. provides, the seller may exercise his lien even though he holds the goods as an agent or bailee of the buyer.

(f) *Bombay Steam N. Co. v. Ramdas*, 14 Bom. L.R. 532.

(g) *Anglo Indian Jute Co. v. Omademull*,

38 Cal. 127.

(h) *Bharucha v. Wadilal*, 28 Bom. L.R. 777 (P.C.).

Once the seller parts with possession of the goods to the buyer, however, his lien will not revive on the buyer re-delivering the goods to him for any particular purpose (i).

Part Delivery: Where the unpaid seller has made part delivery of the goods, he can exercise his lien on the balance in hand unless the part delivery is made in circumstances showing that the lien was waived (sec. 49). Thus where the sellers sold a parcel of hops which contained two kinds of hops, viz. 12 packets of "Kent hops" and 10 packets of "Sussex hops", but rendered one invoice for the whole, and after the first kind of packets were delivered, the buyer became bankrupt, *held*, the delivery of a part of the parcel was not intended to be a delivery of the whole and the sellers could therefore exercise their lien as regards the remaining packets (j).

Stoppage in transit (secs. 50-52)

This right is exercisable by the seller under sec. 50 only if the following conditions are fulfilled: (i) The seller must be unpaid. (ii) He must have parted with the possession of the goods. (iii) The goods must be in transit. (iv) The buyer must have become insolvent. (v) The right is "subject to the provisions of the Act". In other words, the seller must not be prevented by other provisions of the Act from exercising the right, e.g. by the bill of lading coming into the hands of the buyer, and by the buyer pledging the goods or selling them to a *bona fide* transferee for value (see sec. 53). The right of stoppage means the right to stop further transit of the goods, and to resume possession thereof and to retain the same till the price is paid.

The right of stoppage in transit is thus distinguished from the seller's lien: (i) It comes into operation only after the seller has parted with the possession of the goods; the seller's lien on the other hand comes into existence and continues so long as the seller has got possession of the goods. (ii) The right of stoppage in transit arises only where the buyer has become insolvent; the seller's lien is available to him in all the various cases mentioned in sec. 47. Notice that both the rights are available to the unpaid seller though property in the goods has passed to the buyer.

Duration of transit (sec. 51)

Under sec. 51 goods are deemed to be in transit from the time they are delivered to a carrier or other bailee for the purpose of transmission to the buyer, until the buyer or his agent in that behalf takes delivery thereof from the carrier or other bailee (cl. 1).

In an English case (k) buyers, who had bought goods from Messrs. Clark and Co. of Wolverhampton, instructed the sellers to send the goods by a certain named ship to Melbourne. Goods were first railed to London and then shipped to Melbourne, a Mate's receipt being sent to buyers. On the buyers becoming insolvent, the sellers gave notice to the Rail Co. to stop delivery to the buyers, but it was too late. They then gave fresh notice to the shipowners claiming back the goods before the ship arrived at Melbourne. On arrival there, the trustee in bankruptcy of the buyers demanded the bills of lading from the Master. *Held*, the goods having been effectively stopped in transit, the trustee could not claim them.

(i) *Valpy v. Gibson*, 4 C.B. 837.

(j) *Miles v. Gorton* (1834), 2 Cr. & M.

504.

(k) *Bathell v. Clark*, 19 Q.B.D. 553.

(i) If the buyer or his agent lawfully obtains delivery of the goods before they arrive at their destination, the transit is at an end. Cl. (2): The possession must be obtained by the buyer or his agent with the consent of the carrier (*l*).

(ii) If after arrival of the goods at their appointed destination, the carrier or other bailee acknowledges to the buyer or his agent that he holds the goods on his behalf and continues to hold them accordingly, the transit is at an end and it is immaterial that the buyer has indicated a further destination. Cl. (3): Notice that mere arrival of the goods at the destination does not end the transit. There must be delivery to the buyer or his agent thereafter or the carrier must have attorned to the buyer before arrival at destination (*m*).

(iii) Where the carrier or other bailee wrongfully refuses to deliver the goods to the buyer, the transit is at an end.

(iv) On the other hand, where the buyer rejects the goods and the carrier or other bailee continues in possession of them, the transit is not deemed to be at an end, though the seller may have refused to take back the goods.

(v) Where the goods are shipped per ship chartered by the buyer, it is a question depending on the facts of each case, whether they are in possession of the master as carrier or as agent of the buyer. Cl. (5): Where bills of lading are taken by the seller for delivery to his "order or assigns", the carrier will be regarded as agent of the seller though the ship belongs to the buyer. It is otherwise, when bills of lading are taken for delivery to buyer or assigns (*n*).

(vi) Part delivery of the goods to the buyer or to an agent on his behalf does not prevent the seller from exercising the right against the balance of the goods, unless part delivery shows an intention to waive the right.

(vii) Notice that if the buyer after the transit has started, directs the goods to be taken to a place other than their original destination, transit continues.

(viii) Delivery to master is not delivery to the buyer, if the seller reserves the right of disposal to himself, even if the ship is chartered by the buyer.

Right of stoppage, how exercised (sec. 52)

The unpaid seller may exercise the right of stoppage in transit, (i) by actually taking possession of the goods, or (ii) by giving notice of his claim to the carrier or other bailee in whose possession the goods are. Such notice may be given to the person in whose actual possession the goods are, e.g. the master of a ship or to his principal, i.e. the shipowners. In the latter case, notice must be given in sufficient time to enable the principal to

(*l*) *Whitehead v. Anderson* (1842), 9 M. & W. 518.

(*m*) *Bathell v. Clark* (supra).

(*n*) *Shotsmans v. L. & Y. Rly. Co.*, L.R. 2 Ch. App. 332.

communicate the same to his agent, so as to prevent delivery to buyer. When notice is given to the carrier or other bailee in possession of the goods, he is bound to deliver the goods to or according to the directions of the seller at the latter's expense. If the bailee acts otherwise, he so acts at his peril. His only mode of protecting himself is to take an indemnity and if that is refused, to file an interpleader suit (o).

Notice that a simple notice to the carrier forbidding delivery is sufficient exercise of the right of stoppage. The effect of the notice is to re-vest the possession in the seller, so that if the carrier thereafter delivers the goods to the buyer, he is guilty of conversion. A demand for return of a bill of lading which has been kept as security by the shipowner, has been held to be sufficient exercise of the above right (p).

Effect of sub-sale or pledge by buyer (sec. 53)

The seller's right of lien and of stoppage in transit are effectual against all persons who acquire an interest in the goods, with notice of the rights. Any sale or other disposition of the goods by the buyer, therefore, does not destroy the rights.

Exception, however, is made in two cases by sec. 53: (i) where the seller assents to such disposition, and (ii) where a document of title to the goods has been lawfully assigned or transferred to any person as buyer or owner thereof and such person transfers the document to another, who takes it in good faith and for value, then, if the disposition is by way of sale, the unpaid seller's rights are defeated and if it is by way of pledge or other disposition for value, the unpaid seller's rights take effect, only subject to the right of the pledgee or the transferee. (iii) A third rule is added to the last as a rider: Where the transfer is by way of pledge and the pledgee holds other securities from the transferor as security for the same debt, the unpaid seller may require the pledgee to go first against the other securities as far as possible. This is called the "right of marshalling securities" which an unpaid seller has got when the goods sold by him are pledged by the purchaser to secure past or present advance made by the pledgee to him.

In a Bombay case, C purchased cotton from R at Bagalkote. The cotton was to be sent by rail and sea to C at Bombay. The Railway Co. passed receipts for mixed travel by land and sea in favour of C. C drew hundis for payment of price in favour of R. Subsequently, C in consideration of advances from S, assigned the railway receipts to S by endorsement, while the cotton was in transit. C thereafter became insolvent and the hundis were dishonoured. R thereupon wired to the Steamship Co. not to deliver the goods to C. Held, by the Privy Council in a contest between R and S, that as railway receipts were "documents of title" and as by endorsement they had been validly pledged by C with S as security for advances specifically made against them, R could not stop them in transit without payment to S of the amount due to S under the pledge (q).

Notice that a sub-sale by the buyer with the assent of the seller will defeat the seller's lien and right of stoppage, but not a mere acknowledgment by the seller of the buyer's sub-contract (r). Similarly, under the proviso, the transfer of the document of title to the buyer must be lawful.

(o) *Bapuji v. Clan Line Steamers*, 11 Bom. L.R. 1250.

(p) *Litt v. Cowley* (1816), 7 Taunt. 169.

(q) *Ramdas v. Amarchand & Co.*, 18 Bom. L.R. 670.

(r) *Morduant v. British Oil Cake Mills* (1920), 2 K.B. 502.

Secondly, the buyer must have transferred it to another who takes it for value and without notice of the seller's lien. It is then only that the unpaid seller's rights are defeated (s).

Effect of exercise of rights of lien or stoppage in transit

As sec. 54, cl. 1, provides, a contract of sale is not rescinded by the mere exercise of the unpaid seller's right of lien and stoppage in transit. In other words, in spite of the retaking of possession of the goods by the seller, the buyer is still entitled to perform the contract, if he chooses to do so. Similarly, the seller also remains liable to perform his part of the contract. On the other hand, the exercise of the right in question by the seller may be accompanied by circumstances which make it clear that the parties have treated the contract as at an end. It is a question of fact in each case.

Seller's right of re-sale (sec. 54, cls. 2-4)

Under cl. 2 of sec. 54 (i) where the goods are perishable or (ii) where the unpaid seller has exercised his right of the lien or stoppage in transit, he can give notice to the buyer of his intention to re-sell the goods. If after such notice, the buyer does not within reasonable time, pay or tender the price, the seller can, within a reasonable time, re-sell the goods and recover from the original buyer any loss occasioned by the breach. If any profit results on such re-sale, the seller will be entitled to take it. If the unpaid seller fails to give such notice, he is not entitled to recover damages against the buyer but on the other hand shall be accountable to him for the profit, if any, on such re-sale. The title of the purchaser at such re-sale is not affected by the fact that notice of the re-sale has not been given by the unpaid seller to the original buyer (cl. 3).

Notice that the above clauses deal with cases where the property has passed to the buyer. In such cases, a statutory right of re-sale is given to the unpaid seller, which he can exercise only in the two cases mentioned above, subject to the conditions therein laid down.

"Perishable" in cl. (2) is not confined to physical deterioration; it also includes commercially perishable goods, and goods liable to deterioration so as to make them unmerchantable (t). The measure of damages in case of re-sale under these clauses is the difference in the contract price and the price realised on such re-sale plus the expenses of re-sale. The seller must exercise his right of re-sale within a reasonable time. A delay of eight months has been held to be unreasonable (u). It has been recently held in England that where the seller exercises his right of re-sale under cl. 2 above, he does not thereby rescind the contract but on the contrary, affirms it. Any deposit therefore made by the purchaser, cannot be forfeited by him, but must be brought into account in any claim for damages made by him under the cl. (v).

(iii) A third right of re-sale arises, under cl. (4) of the sec., where by the contract, the seller has expressly reserved a right of re-sale in case the buyer makes default. In such case also, the seller can re-sell the goods, although the property in the goods has passed to the buyer. When, however,

(s) *Kemp v. Folk* (1882), 7 App. C. 573.

(t) *Asfar v. Blundell* (1896), 1 Q.B. 123.

(u) *Parthasarathi v. Gopinath*, 48 Mad.

787.

(v) *Gallacher v. Shilcock* (1949), T.L.R.

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the seller exercises his right of re-sale under this clause, the original contract is rescinded, but without prejudice to the seller's right to recover damages for its breach. The right of re-sale given by cl. 4 is exercisable by the seller, even where property has not passed to the buyer (*w*). Before such right of re-sale can be exercised, however, it is necessary that the goods have been appropriated to the contract (*x*).

Notice that where such re-sale is by auction, it is competent to the seller to buy the goods himself (*y*). Further, the re-sale must be within a reasonable time. If there is too much delay, the seller will be relegated to his usual remedy of damages on the basis of the difference between the contract price and the market price on the date of the breach (*z*).

Rights of unpaid seller against buyer personally (secs. 55-56)

The unpaid seller has further rights against the buyer personally also. They are: (i) a right to sue for the price, (sec. 55) and (ii) the right to sue the buyer for damages for non-acceptance (sec. 56).

As to (i), sec. 55 provides that (a) where under a contract of sale, the property in the goods has passed to the buyer and the buyer wrongfully refuses or neglects to pay for the goods in accordance with the terms of the contract, the seller can sue him for the price; (b) where, under the contract, price is payable on a certain day, irrespective of delivery and the buyer wrongfully refuses or neglects to pay the same, the seller can sue for the price though the property has not passed to the buyer and the goods have not been appropriated to the contract.

Notice that the second case gives the seller a right to sue for the price, although the property has not passed to the buyer. Generally, where property has not passed, the seller's right is only to sue for damages for non-acceptance which is given by sec. 56, where the buyer wrongfully refuses or neglects to accept the goods.

Buyer's rights against seller (sec. 57)

Where the seller wrongfully neglects or refuses to deliver the goods to the buyer, the buyer has (i) the right to sue the seller in damages for non-delivery. Notice that where property has passed to the buyer he has got another right also, viz. (ii) a right to sue for specific performance. This right is given by sec. 57 of the Act and its limits are regulated by the Specific Relief Act. The decree for specific performance, when such relief can be had, may be unconditional or upon such terms as to damages, payment of price or otherwise as the Court thinks just.

(iii) Where a warranty is broken by the seller, or where the buyer is compelled to treat a breach of condition, as a breach of warranty, the buyer may (a) set up the breach of warranty in diminution or extinction of the price, or (b) sue the seller for damages for breach of warranty (sec. 59). In case of an anticipatory breach of contract by the seller or the buyer, the other party may treat the contract as subsisting till the date of performance arrives or may treat the contract as broken at once and sue for damages on

(*w*) *Moll Schuttler Co. v. Luchmi Chand*,
25 Cal. 505.

(*x*) *Anguila v. Sassoon & Co.*, 39 Cal. 568.

(*y*) *Ratanlal v. Tekchand* (1930), A.I.R.
Lah. 379.

(*z*) *Goorla Mills v. Vallabhdas*, 27 Bom.
L.R. 1168.

that footing (sec. 60). The right of either party to sue for interest or special damages is not affected by the above cl. nor the right to recover money paid as on a consideration which has failed.

Interest as damages (sec. 61): In absence of a contract to the contrary, the Court may award interest at such rate as it deems fit on the price (i) to the seller in his suit for price, from the date of tender of the goods or the date fixed for payment of price; (ii) to the buyer, in his suit for refund of prepaid purchase price, from the date of payment thereof.

Interest is recoverable on damages, only if the case falls under the Interest Act of 1879. Under this Act, interest is recoverable at the current rate (i) on all debts or sums certain payable at a certain time, from the time demand is made, with claim of interest from date of demand and (ii) on all debts or sums certain not payable at a certain time, from the time the demand for payment is made in writing with claim for payment of interest from date of demand.

Sale by auction (sec. 64): In case of a sale by auction, (i) where goods are put up for sale in lots, each lot shall be, *prima facie*, regarded as a separate contract of sale; (ii) the sale is complete when the auctioneer announces its completion by fall of the hammer or otherwise; till then any bidder may withdraw the bid; (iii) a right to bid may be expressly reserved by or on behalf of the seller, in such a case only, can the seller bid at the auction; (iv) if a sale contravenes the above rule, it can be treated by the buyer as fraudulent; (v) a sale may be notified subject to a reserve or upset price; (vi) if the seller makes use of pretended bidding, the sale is voidable at the option of the buyer.

Notice that the mere fact that there is a reserve bid does not entitle the seller to bid. If the buyer, after the lot is finally knocked down to him, fails to pay the price and goods are re-sold under the conditions of sale, the buyer is still liable for the price. A combination of persons not to bid against each other at an auction (called knock-out) is not illegal (a).

CHAPTER XI

PARTNERSHIP

HISTORICAL RETROSPECT: The law relating to partnership in India is contained in the Indian Partnership Act (IX of 1932). The law on the subject was originally contained in and formed part of the "Indian Contract Act" as Ch. XI thereof. As various amendments were desired to be made and certain points with regard to partnership law were required to be clarified, Chapter XI of the Contract Act was repealed and a new and comprehensive legislation was passed in 1932 which is the "Indian Partnership Act".

Scheme of the Act: The Partnership Act is an attempt to lay down in succinct form the principal rules of law relating to partnership. The Act when passed, had one peculiarity, viz. that whereas all secs. but one of the Act came into force with the passing of the Act, i.e. on 1st October 1932, the operation of sec. 69 was postponed to 1st October 1933, i.e. for one year after the passing of the Act (sec. 1). The reason for so doing was to familiarise

(a) Jyoti v. Jowmull, 36 Cal. 134.

people with the meaning and ambit of the principle of registration, which for the first time introduced by the Act into India. The Act is an amending and defining Act", as declared by the preamble and is, therefore, not to be treated as exhaustive. It is not retrospective also, except as provided by sec. 74. As sec. 3 distinctly mentions, the unrepealed provisions of the "Contract Act", except so far as inconsistent with the express provisions of the present Act, are not repealed thereby.

What is partnership (secs. 4-6)

A partnership is defined by sec. 4 as "the relation subsisting between persons who have agreed to share the profits of a business, carried on by all or any of them acting for all". As the definition shows, a partnership consists of three essential elements: (i) it must be the result of an agreement between several persons, (ii) the agreement must be to share the profits of a business and (iii) the business must be carried on by all or any of them acting for all.

All the three above essentials must exist before a partnership can come into existence. As to (i), notice that a partnership cannot be the result of status but only of a contractual agreement between the various parties. This is pointed out by sec. 5, which further goes on to say that the members of an undivided Hindu family carrying on a joint family business are not necessarily partners. The reason is that as a result of the peculiarities of Hindu Law relating to joint family, a male child of a Hindu acquires an interest in such business by birth, apart from any agreement in that behalf. Similarly, as a result of the peculiar rules of Burmese Buddhist Law, a Burmese Buddhist husband and wife become on marriage joint owners of a business which they or any of them are conducting. In these two cases, there being an absence of a contractual agreement between the parties to form a partnership, they are not regarded by law as partners. Of course, this does not mean that there can be no partnership between members of a joint Hindu family to carry on a family business in partnership. But where such a fact is alleged, it will be required to be established by proper evidence in the light of the above definition. Notice further that partnership requires an agreement between at least two persons. Thus there can be no partnership consisting of a single individual, though under the special provisions of the Civil Procedure Code, such an individual, if carrying on a business in a name other than his own, can sue in the firm name (Civil Procedure Code, O. 30, r. 10).

The second requirement of the definition is that the persons should have agreed to carry on business and share the profits thereof between them. Carrying on a business is really the most important part of the definition of partnership. "Business" here includes any trade, occupation or profession [sec. 2, cl. (b)]. Unless the combination, however, is for the purpose of carrying on a "business" (and sharing the profits therein), it will not amount in law to a partnership. It is this element which distinguishes a partnership from "co-ownership". Both involve joint ownership of property, but whereas in partnership, the joint ownership is with a view to carry on a business, there is no such end in view in the case of co-ownership. This is why co-owners are not partners.

Co-ownership is distinguished from partnership in the following particulars: (i) Partnership is necessarily the result of agreement, co-

ownership is not, e.g. where A and B inherit property from C as co-heirs. (ii) Partnership necessarily involves working for profit, co-ownership does not. (iii) A partner cannot transfer his share to an outsider, without the consent of the other partners. A co-owner can always do so. (iv) A partner is the agent of the other partners to bind the firm, a co-owner is not. Thus joint owners of a house, which is let out to tenants and who divide the net receipts between themselves in fixed proportions are not partners. Similarly, where two persons purchased a tea shop jointly and let it out to a third person, dividing the rent between themselves proportionately, it was held that they were not partners, but co-owners only, of the shop (b). On the other hand, if the same persons combine together for the purpose of buying properties and letting them out to tenants and sharing the profits thereof between themselves, they will not be co-owners but partners.

Further, a joint carrying on of a business alone, is not enough; there must be an agreement to share the profits. Thus if A and B agree to work together as carpenters and the agreement further provides that A shall receive all the profit and B shall only receive wages for his services, it cannot be said that A and B are partners. Notice in this connection, however, that a person may be admitted into a partnership with an agreement that he shall receive a fixed salary in lieu of his share in the partnership profits. Such a person would be a partner (c).

Notice further that though sharing of profits is one of the elements of a partnership and often affords cogent evidence of partnership, participation in profits is, by no means, a conclusive test of the existence of a partnership. This is clearly pointed out by expl. 2 to sec. 6. Thus a lender of money to persons engaged or about to be engaged in a business as partners, is not necessarily a partner, because he receives a share of the profits of the business as consideration or part consideration for the loan (d). Similarly, a servant or agent who receives a share of profits as his remuneration, the widow or child of a deceased partner, who receives such share by way of annuity and the seller of the goodwill of a business who is given a share of profits as consideration for sale of the goodwill, are not, by reason of such facts alone, liable as partners.

The third requirement is that the business must be carried on by all or by any of them on behalf of all. This feature underlines the cardinal principle of partnership law, which is that every partner is, by law, an agent of the other partners and of the partnership, of which he forms a member. Thus it is possible to have a partnership, in which one or some of the partners have the sole right of management and control (e). Similarly, a partnership is possible with a "sleeping" or "dormant" partner or partners (see seq.).

Notice that executors carrying on business under the terms of a testator's will are not partners (f). The question is always one of intention (g). It has been recently held by the Lucknow High Court (h) that where certain

(b) *Govindan Nair v. Nagabhushanamal*, A.I.R. (1948), Mad. 343.

(c) *Raghunandan v. Hormusji*, 51 Bom. 342.

(d) *Mallow March & Co. v. Court of Wards* (1872), L.R. 4 C.P. 419.

(e) *In re Ambalal Sarabhai*, 25 Bom. L.R. 1225.

(f) *Re Fisher & Sons* (1912), 2 K.B. 491.

(g) *Walker v Hirsch* (1884), 27 Ch.D. 460.

(h) *Sarna v. Ruban*, 21 Luck. 285.

persons agree to form a managing agency firm of a limited company about to be floated, there is no partnership, before the limited company comes into existence. Similarly, promoters associated for the purpose of floating a company, the managing agency whereof they intend to acquire and carry on in partnership, are not partners. Their relations *inter se* can only be determined by the law of contract (h). A single venture may also amount to a particular partnership under sec. 8; e.g. an agreement between several persons to purchase lac, to be auctioned at different dates, and to sell the lot subsequently and to divide the profits (i).

Firm and Firm name (sec. 4): The body of persons who have combined together to carry on a business in partnership are collectively called a "firm" and the name in which they carry on the business is called the "firm name" (sec. 4).

Notice that though in common language, a "firm" is regarded as something distinct from the partners comprising it, in law it is not so. As James L.J. says in *Ex parte Corbett* (1880), 14 Ch.D. 122, for the purpose of determining legal rights "there is no such thing as a firm known to law". A firm is nothing more than a compendious name of the partners forming it, though for certain procedural reasons, a right is given to partners to file a suit in the firm name and it is further provided that partners can also be sued in the firm name under certain conditions (O. 30, Civil Procedure Code).

As regards the "firm name", notice that under sec. 58, a firm name which is desired to be registered should not contain words like 'Crown', 'Royal', 'King', etc. showing Royal or Government patronage, except with the written consent of the State Government. A firm name should not be such as would mislead others into believing that it is another firm and thus induce them to enter into transactions with the first firm on that basis. This is called "*passing off*", which is an actionable wrong.

Registered Partnership

The Act introduces an innovation, so far as partnership law in India is concerned: this is the new provision for registration of partnerships contained in secs. 56-71 of the Act. Under these secs., the partnership firms are bound to get themselves registered with the Registrar of Partnerships for certain purposes and under certain conditions. These provisions had no counterpart under the old law. For this reason, in order to accustom the people to the meaning and effect of the new provisions, sec. 1, cl. (3) of the Act, expressly postponed the application of sec. 69 of the Act (which deals with the effect of non-registration of the partnership) till 1st October 1933, while the rest of the Act was made operative from 1st October 1932. A registered partnership, therefore, is a partnership which is registered under the Act.

Registration of firms and of incorporated companies distinguished

It should be observed, however, that the registration of partnership firms with the Registrar of Partnerships and the registration of companies with the Registrar of Companies under the Indian Companies Act are two entirely different things. Thus (i) the registration of a partnership firm is

optional, the registration of an incorporated company is compulsory; (ii) non-registration of a partnership firm does not prevent the firm from functioning; in case of companies, no company can acquire legal existence till it is duly registered as required by the Companies Act; (iii) a partnership which is not registered does not, on that account alone, become an illegal partnership; a company which is compulsorily required to be registered and which is not registered, becomes an illegal association. (iv) The purpose and object of registration in both cases is different. In case of partnership, registration is required in order to secure the necessary evidence of its character and composition. In case of companies, it is the very foundation of their legal existence.

Illegal partnership

A partnership may be illegal in either of two ways: (i) by being formed to carry on an illegal business, e.g. a lottery or (ii) by not being registered when compulsorily required to do so, under the Indian Companies Act. This has reference to sec. 11 of the latter Act, which in effect provides that an association of more than 10 persons in case of banking and of more than 20 persons for other businesses, the object of which is the acquisition of gain, cannot be formed unless such associations are registered under the Companies Act. The number of persons who can form a partnership is thus restricted to 20 in ordinary cases and to 10 in case of banking business.

Notice that there is nothing to prevent an illegal partnership from being sued (j), though, of course, a person who entered into a contract with such a partnership with knowledge of its illegality cannot sue on such contract.

Partnership distinguished from joint family business: The main points of distinction are: (1) a partnership is a result of an agreement between the partners, a joint family business results from status, i.e. from the position given by the personal law of Hindus, to members of a joint family carrying on a family business; (ii) death of a partner dissolves a partnership, it is otherwise with regard to a joint family business. (iii) The management of a joint family business generally remains with the Karta, the senior male member of the family. In a partnership, all partners are equally entitled to take part in the partnership business. (iv) A member of a joint Hindu family on separation is not entitled to ask for past accounts. It is otherwise in case of a partnership. (v) A member of a joint Hindu family is liable for the debts of the business only to the extent of his interest in the joint family property unless he himself is a contracting party; a partner is jointly and severally liable for the partnership debts. Notice that when a Karta of a joint Hindu family enters into partnership with a stranger, the other members of the joint family do not *ipso facto* become partners also (k).

EVIDENCE OF PARTNERSHIP (sec. 6): Under this sec., in determining whether a particular group of persons constitutes a partnership, regard is to be had to the real relation between the parties as shown by all relevant facts taken together. The question whether a particular group of persons constitutes a partnership or not, is often a difficult one to decide. No general rule can be laid down in this connection, except the one mentioned above. No doubt, sharing of profits will be an important criterion but as laid down by the House of Lords in *Cox v. Hickman* (l), it is not conclusive. Taking part in the conduct of the business is another important element to be considered, though with a similar qualification. The books of account will usually give a good indication as to

(j) *Brahmayya v. Hamiah*, 43 Mad. 141.

(k) *Lilabati v. Lalit Mohan*, A.I.R. (1952)

Cal. 499.

(l) (1860), 38 H.L.C. 268.

whether the parties are partners or not. The reason is that partnership accounts are generally maintained in a different way than is the case where one or more of the parties are lenders. Even this however is not an infallible guide. As the sec. says, all the relevant facts must be scrutinised in each case in order to determine whether a particular set of persons are partners or not. Notice that the use of the word "partner" does not make a partnership, when there is none in fact (m).

Thus where a plaintiff who was the sole owner of a solicitors' firm entered into an agreement with the defendant under which he "agreed to admit" the defendant "as a partner in the said firm" for the period of one year, and, it was further agreed that the defendant on the termination of the said period was not to have any claim or interest in the firm and its outstandings, property, name and goodwill and that the defendant was to receive in lieu of his share in the profits a fixed sum of Rs. 500 per month and that he was not to be liable for the losses or the liabilities of the firm, *held*, the defendant, under the terms of the agreement, had become a partner and was not an employee of the firm (m). On the other hand, where a Mahomedan lady inherited a large sum from her father which she invested in securities from which she got an income of Rs. 74,000 per year and then she entered into a partnership with her minor children to divide the profits in certain proportions, *held*, there was no partnership between the parties (n).

Joint venture (sec. 8): Where persons jointly carry out particular adventures, they are called joint adventurers and are regarded in law as partners (sec. 8), e.g. a group of persons buying up a particular lot or lots at auction, with a view to re-sell at a profit.

Kinds of partnership (sec. 7): Partnerships can be of two types: (i) partnership at will and (ii) partnership for a fixed term. Sec. 7 provides: "where no provision is made by partners for the duration of the partnership or for its determination, it is called partnership at will". Such a partnership can be dissolved by a simple notice in writing as provided by sec. 43, while the other kind of partnership can be dissolved only under certain conditions and by following certain procedure (see seq.).

Duties of partners to one another (secs. 9-13)

These secs. are an attempt to formulate in simple language, the partners' duties *inter se*. Two fundamental duties are laid down first. These are: (i) Partners are bound to carry on the business of the firm to the greatest common advantage, to be just and faithful to each other and to render true accounts and full information of all things affecting the firm to every partner and/or his legal representative (sec. 9). The sec. postulates complete loyalty between partners in carrying out the business of the firm.

(ii) A partner is bound to indemnify the firm for loss caused to it by his fraud in the conduct of the business of the firm (sec. 10), e.g. if he misappropriates moneys paid to him on behalf of the firm by a third person. Notice that the above two secs. create an absolute liability from which* therefore, it is not possible for any partner to contract himself out, by special agreement.

Apart from these two fundamental rules, the rights and duties of partners *inter se*, may be determined by any contract between the partners (sec. 11), i.e. by any agreement which the partners may choose to enter into between themselves, generally called "partnership articles".

(m) Raghunandan v. Hormusjee, 51 Bom. 342.

(n) Re Sakinaboo, 34 Bom. 55 Bom. A.C. 7.

contract may be express, i.e. in writing or oral or may be implied, i.e. may be inferred from a long course of dealing between the partners. Such a contract can also be varied by consent of all partners (which consent, again, may be either express or implied) [sec. 11, cl. (i)]. As sub-sec. 2 of sec. 11 provides, a special provision in the partnership articles that no partner shall carry on any other than the partnership business is not void as being in restraint of trade, as defined by the Contract Act (sec. 27). Notice that consent of all the partners is required to vary or change the partnership articles.

Having laid down the above general rules, secs. 12 and 13 proceed to lay down certain special rules which are to operate "subject to contract between the partners", i.e. if the partnership articles do not otherwise provide. These are: (i) each partner is entitled to take part in the conduct of the business of the firm; (ii) each partner is bound to attend diligently to the partnership business; (iii) on a difference arising between the partners with regard to the business of the firm, it shall be determined according to the view of the majority but (iv) no change in the business of the firm can be introduced without the consent of all partners; (v) each partner is entitled to have access to, inspect and take copies of the books of account of the firm (sec. 12).

As the sec. points out, however, these duties and rights can be always varied by consent. In a Privy Council case (o), their Lordships allowed a special allowance to a partner on whom the whole burden of carrying on the partnership business was thrown, by the other partner not being diligent at all in the conduct of the partnership business. Notice that the privilege of having access to and of inspecting and taking copies of the books of the firm given to a partner by the sec. can be exercised by him through a duly authorised agent, but it should not be abused by him, i.e. should not be used by him to cause injury to the firm. If he does, he will be restrained by an injunction (p).

Other rights and liabilities of partners are defined by sec. 13. These are, "subject to contract between the partners", as follows: (vi) no partner can claim remuneration for taking part in the business of the firm; (vii) partners entitled to share profits equally are bound to share the losses also in the same manner; (viii) when interest is payable to a partner under the partnership articles, on capital subscribed by him, such interest is payable only out of profits. (ix) As regards advances made by a partner to the firm, apart from contribution of capital, such partner is entitled to claim interest thereon at 6 per cent per annum.

(x) Certain mutual indemnities are also provided for by the sec. They are: (a) the firm is bound to indemnify a partner in respect of payments made and liabilities incurred by him in the conduct of the ordinary business of the firm and for doing an act in an emergency for protecting the firm from loss, if it is such as a prudent man would do in his own case, under similar circumstances. (b) A partner is bound to indemnify the firm for loss caused to it by his wilful neglect in the conduct of the business of the firm (sec. 13).

Notice that items (vi) to (x) can always be varied by express agreement. They very frequently in fact are: thus a managing partner may be

(j) *Brahmayya v. Shēkarasah*, 22
(k) *Lilabati v.*

(p) *Trego v. Hunt* (1896), A.C. 7.

given a salary over and above his share ; the shares of partners also may be unequal. Notice also that under the last clause of the sec. 13, viz. cl. (f), a partner is liable to indemnify the firm in case of "wilful neglect" only, which means "doing of a wrongful act deliberately, i.e. knowing that the same is wrong". Apparently, no indemnity is payable in respect of simple negligence, e.g. an error of judgment.

Partnership property (sec. 14)

The sec. lays down that "subject to contract between the partners", "partnership property" includes, viz. (i) property originally brought into the firm, with all property, rights and interest therein ; (ii) property acquired by purchase or otherwise by the firm ; (iii) property similarly acquired (by any individual or more partners) for the purpose of and in the course of the business of the firm and (iv) goodwill of the firm.

The sec. in cl. (2) goes on to lay down a rule of presumption, viz. that unless a contrary intention appears, property acquired with partnership moneys is presumed to be acquired for the firm, i.e. to be partnership property.

The question of what is "partnership property" becomes important when disputes arise between partners on or after dissolution and when execution is sought to be levied against such property by a creditor of the firm. The mere fact that the property of a partner is being used for the purposes of the firm does not *ipso facto* make it partnership property (q). It is always a question of intention, to be spelt out from various incidental surrounding circumstances. Thus if the value of the property is credited in the partnership books to the account of the particular partner as his capital contribution, the property will be partnership property (r). Similarly, if property is bought in the name of a partner and the price thereof is paid out of partnership moneys, the property will be partnership property (s). In a Bombay case (t) two parties effected insurance on their lives for the benefit of the partnership and paid the premium out of partnership funds. *Held*, the policies formed part of the partnership assets (t).

"Goodwill" has been always difficult to define. It has been described as "the whole advantage, whatever it may be, of the reputation and connections of the firm" (u). It means the value which a business has obtained by long continuance, in the shape of connections with customers and the public generally. The important point to notice is that "goodwill" is now clearly an "asset" and sometimes a most valuable asset. See sec. 55 for the effect of the sale of a goodwill. Goodwill can be sold along with the business or separately. Notice that under sec. 15 the partnership property can be used by the partners for partnership purposes only, unless there is a contract to the contrary.

Partners' personal profits (sec. 16)

The sec. lays down that, unless the partnership articles otherwise provide, (i) no partner can derive any profit for himself out of a partnership

(q) *Davis v. Davis* (1894), 1 Ch. 393.
 (r) *Robinson v. Ashton* (1875), L.R. 20
 E.Q. 25.
 (s) *Nirat v. Burnard* (1827), 4 Russ. 247.

(t) *Re Adarji Mancherji Dalal*, 55 Bom.
 795.
 (u) *Treggo v. Hunt* (1896), A.C. 7.

transaction or from use of the partnership property or connection or name. If he does, he is accountable to the partnership for the same. (ii) Similarly, a partner cannot carry on another business of the same nature as and competing with that of the firm. If he does, he is accountable to the firm for all profits thereof.

The first prohibition results from each partner being an agent of the partnership. As regards the second, notice that with the knowledge and consent of other partners, a partner can carry on a distinct though similar business.

Change in the constitution of the partnership (sec. 17)

A change may occur in the constitution of a partnership in either of four ways: (i) by new partner or partners coming in; (ii) by some partner or partners going out, i.e. by death or retirement; (iii) by the firm being carried on after expiry of the fixed term; and (iv) by the partnership carrying on businesses other than those for which it was originally formed.

The sec. lays down that, subject to a contract to the contrary, in the cases (i), (ii) and (iv) above, the rights and obligations of partners *inter se* remain the same as they were before, so far as may be; as regards (iii), the same rule applies, except that the rights and obligations remain the same, only so far as is consistent with a partnership at will.

Thus where a partnership entered into under articles signed by all the partners, is continued after the death of a partner, the partners surviving will, in absence of a fresh agreement varying the original one, be deemed to be governed by the terms of the original partnership agreement (v). On the other hand, the original terms will be deemed to be varied, so far as is inconsistent with a partnership at will, when a partnership is continued beyond the fixed period. Thus where a partnership deed provides that a partner can dissolve the partnership after notice of a fixed period, such a term would not be applicable, if the partnership continues beyond the original term, because such a term is inconsistent with a partnership at will (w). On the other hand, a clause in partnership articles to refer all disputes to arbitration (x) or to allow a partner to buy a retiring partner's share at a valuation (y) has been held to be applicable in such cases.

Rules as to relation of partners with third persons (secs. 18-30)

These secs. deal with important questions which frequently arise when an act is done by a partner on behalf of the partnership, which gives rise to legal rights and obligations between the partnership on the one hand and a third party on the other. Sec. 18 lays down the fundamental rule of the law of partnership, viz. that subject to the provisions of the Act, a partner is the agent of the firm for all purposes of the business of the firm. This being the rule, the question arises, what is the extent of a partner's authority, so as to make his act binding on the firm. This subject is considered in the secs. following.

Authority of a partner (secs. 19-22)

A partner's authority may be either (i) *express* or (ii) *implied*. It is "express", when it is fixed between the partners by mutual agreement,

(v) *King v. Chuck*, 17 Beav. 325.

(w) *Featherstone v. Fenwick*, 17 Vcs. 307.

(x) *Gillet v. Thornton*, L.R. 19 Eq. 599.

(y) *Essex v. Essex*, 20 Beav. 442.

verbal or written. It is "implied", when there is no express agreement between the partners, in which case, the law impliedly gives certain powers to a partner and also similarly negatives certain other powers as regards a partner.

Implied Authority of Partner

Sec. 19 deals with the subject of "*implied authority of a partner*". It provides for two rules: (I) The first is an *affirmative rule*. It says that subject to sec. 22, the act of a partner which is done to carry on (i) in the usual way, (ii) the business of the kind carried on by the firm, binds the firm. In other words, if the act of a partner is of a nature (i) which is common in the type of business carried on by the firm, and (ii) is done by him in the usual way of carrying on the firm's business, it will bind the partnership. This makes the whole question depend upon the particular kind of business which a firm is carrying on. If, in such a business, e.g. it is usual to give credit to customers, the giving of credit by a partner to a customer will be binding on the firm. Similarly also, with regard to investment of the firm's moneys. The second requirement is that the act must be done in the usual course of business of the firm, e.g. the goods bought by a partner for partnership purposes in the ordinary way, would make the firm liable to pay for them. Similarly, a negotiable instrument signed by a partner for purposes connected with the partnership will bind the other partners, though their names do not appear thereon (z). On the other hand, an act of a partner which is unconnected with and beyond the usual business of the firm, will not bind the firm. Similarly, acts done by a partner in violation of his duty to the firm, will not bind the firm, even if done in the name of the firm, if the other party to the transaction knows about or co-operates in such breach of duty (a). Thus a partner who signs a bill of exchange in the name of the firm, to raise money for his own private purposes, cannot make the firm liable therefor, if the other party is aware of the fraud (b).

Notice that in connection with a partner's implied authority, decisions have made a distinction between a *trading* and a *non-trading partnership*. A business which involves buying and selling goods is regarded as a trading partnership (c); where the business does not involve buying and selling, it is called a non-trading partnership. Thus a solicitor's firm, a firm conducting a cinematograph theatre (d), a firm of commission agents and brokers (e), of Quarry owners or farmers and a film producing concern, have been held to be non-trading partnerships. A firm doing the business of buying and selling copper vessels has been held to be a trading firm (f). With regard to trading partnership or partnership of a general commercial nature, the law implies a general authority in a partner, to sell or pledge partnership property, to buy goods on account of the partnership, to draw, make, sign, endorse, accept, transfer, negotiate or get discounted bills of exchange, cheques and other negotiable instruments in the name of and on

(z) *Bunarasee Das v. Gholam Hussain*, 13 M.I.A. 358.

(a) *Bank of Australasia v. Breillat*, 6 M.P.C. 193.

(b) *Kendal v. Wood* (1871), 39 L.J. Ex. 167.

(c) *Shrimal v. Kapurchand*, 25 Bom. L.R. 1093.

(d) *Higgins v. Beauchamp* (1914), 3 K.B. 1192.

(e) *Yates v. Dalton*, 28 L.J. Ex. 69.

(f) *Motilal v. Unao Commercial Bank*, 32 Bom. L.R. 1571.

account of the partnership (g). In case of non-trading firms, however, such authority has to be expressly conferred.

(II) Cl. (2) of sec. 19, gives the second or *negative rule*, viz. what the law does not include in the implied authority of a partner. According to the cl., in absence of custom or usage of trade to the contrary, the implied authority of a partner does not empower him (i) to refer a dispute relating to the business of the firm to arbitration; (ii) to open a banking account in his own name on behalf of the firm; (iii) to compromise or relinquish any claim of the firm; (iv) to withdraw any suit or proceeding filed by the firm; (v) to admit liability in a suit against the firm; (vi) to acquire immovable property on behalf of the firm; (vii) to transfer immovable property belonging to the firm; and (viii) to enter into a partnership on behalf of the firm.

The above rule means that for the aforesaid purposes, all partners must join together in order to make such acts binding on the firm or one partner must have been expressly authorised by the others to do any of the above acts on behalf of all. In the absence of the above two requirements being fulfilled, such acts, if done by an individual partner, cannot be binding on the firm. As an instance illustrating the application of the above rule may be cited the case of *Hirachand v. Jayagopal* (h). In this case, on an agreement of sale of certain immovable property, it was discovered while investigating the vendor's title, that the property had once been legally and at another time equitably mortgaged to two distinct firms. The mortgage debts having been paid, the vendor produced, in one case, a release and in the other case, a reconveyance signed on behalf of the said two firms, by a single partner therein. On the purchaser objecting to the vendor's title, it was held that the objection was valid, on the ground that no express authority had been proved with regard to the partner signing and further that an implied authority to transfer immovable property of the firm can hardly be presumed in the case of a partner. Notice that, as has been held in England, no partner, even in a trading firm, has implied authority to give a guarantee in the name of the firm (i). On the other hand, a payment to one partner is a good payment to the firm. Further, a borrowing by a partner in a non-trading firm without express authority, will make the other partners liable therefor, if the amount borrowed has been used for the purpose of the business (j).

Notice that partners may, by mutual agreement, extend or restrict the implied authority of a partner, but so far as outsiders are concerned, they cannot be affected by such limitations unless: (i) they have actual notice of the same or (ii) they did not know or believe that the person was a partner. In absence of these facts, an act of a partner which falls within his implied authority as laid down by sec. 19 binds the firm (sec. 20). Where by a partnership deed, a partner is appointed the general manager of a business, with power "to negotiate with all persons" for the purpose of the business, this gives him the power to negotiate the settlement of a suit against the partnership. No question of implied authority under sec. 19, cl. (2) (c), arises in such a case (k).

(g) *Bank of Australasia v. Breillat*, supra.

(h) 49 Bom. 245.

(i) *Brettell v. Williams* (1849), 1 Ex. 623.

(j) *Reversion Fund Insurance Co. v. Maison Causway* (1913), 1 KB. 634.

(k) *Shahani v. Haverlo Trading Co.*, 51 C.W.N. 488.

(III) Sec. 21 lays down a third rule as regards a partner's authority. It says, "a partner's authority in an emergency extends to do all such acts as are necessary to protect the partnership from loss, as a prudent man, in his own case, would do, under similar circumstances". Notice that under this sec. even unauthorised acts of a partner may be binding on the firm, if they are necessary to meet an emergency.

(IV) The last rule as regards a partner's authority is laid down by sec. 22, which says that in order to bind the firm, the act or instrument done or executed by a partner must be done or executed by him in the firm name or in such other manner as to show an intention to bind the firm. A signature of a partner "per procuratum", i.e. on behalf of the firm, would thus bind the firm.

It has been held in Bombay that in the winding up of a dissolved partnership it is not a necessary act of a partner to create a "novatio" (by taking a Havala of another firm), in respect of a debt owing by a person to the firm. Such Havala is not binding on the other partners unless they have previously consented to it or subsequently ratified it (l). It has been held by the Privy Council that it is competent to one partner in whose name a contract has been entered into, to sue for a debt due to the firm, even though another partner has not joined as party plaintiff (m).

Notice further that where money is borrowed by one partner in the name of the firm but without the authority of the co-partners and the same has been applied in paying off the debts of the firm, the lender is entitled in equity to repayment by the firm of the amount which he can show to have been so applied. The same rule also applies to moneys *bona fide* borrowed and applied for the legitimate purposes of the firm (n).

Effect of admission by partner (sec. 23): An admission or representation made by a partner concerning the affairs of the firm, is evidence against the firm, if made during the ordinary course of its business. The sec. deals with a rule of evidence. Partners, being agents of each other, an admission of liability made by a partner would bind the firm, if made during the course of the firm's business. Of course, it will not be conclusive but it will be admissible in evidence against the partnership.

The question of an acknowledgment signed by a partner with regard to a partnership debt may be considered here. According to the Bombay, Calcutta and Allahabad High Courts, such an acknowledgment by a partner of an ordinary mercantile concern would extend the period of limitation against the firm under sec. 19 of the Limitation Act (o). According to the Madras High Court, however, special authority must be proved (p). Notice that the rules laid down by the sec. do not apply after dissolution of the firm (q).

Effect of Notice to partner (sec. 24): According to sec. 24, notice to a partner, who habitually acts in the business of the firm, of matters relating to the business of the firm, operates as a notice to the firm, except in case of

(l) Kapurji v. Pannaji, 30 Bom. L.R. 1560.

(m) Ajacio v. Forbes, 14 M.P.C. 160.

(n) Laxmiram v. Motiram, 6 Bom. L.R. 1106.

(o) Premji v. Dossa, 10 Bom. 358; Bengal

National Bank v. Jathendranath, 56 Cal. 556; Gadoo Bibi v. Parshotam, 10 All. 418.

(p) Valasubramaniya v. Ramnathan, 32 Mad. 421.

(q) Premji v. Dossa, supra.

fraud committed by or with the connivance of the partner. The notice referred to here is actual and not constructive notice. It must be obtained by a working partner and not a dormant partner. It must further relate to the firm's business. Then alone it is notice to the firm. Thus the knowledge of a partner as to a particular defect in the goods which he is buying for the firm will be knowledge of the firm, although the other partners are, in fact, not aware of the defect. The only exception is in the case of fraud. If, therefore, the purchasing partner, in collusion with the seller, has conspired to conceal the existence of the defect from the other partners, the rule will not operate and the other partners would be entitled, on the defect being discovered by them, to reject the goods.

Liability of partners to outsiders (secs. 25-27)

Secs. 25-27 deal with the question of the firm's liability (i) for contract, (ii) for torts and (iii) for misappropriation of third person's property by a partner.

As regards *contractual liability*, sec. 25 provides that every partner is jointly and severally liable for all acts of the firm while he was a partner. In other words, the liability of partners, e.g. for partnership debts, is both joint and several. The rules laid down by secs. 43-45 of the Contract Act with regard to joint promises will, therefore, apply in that case. According to English Law, the liability is joint only (r).

As regards (ii), i.e. *civil wrongs* or torts, sec. 26 provides that for the wrongful acts and omissions of a partner, acting in the ordinary course of business of the firm, or with the authority of the other partners, causing loss or injury to a third person or causing a penalty to be incurred, the firm will be liable to the same extent as the partner himself, if the partner was acting in the ordinary course of the business of the firm, or with the authority of the other partners. The test is whether the partner was acting in the management of the firm. If he was so acting, loss caused to third persons by his negligence in so doing, will make the firm liable for the loss. Thus it has now been held that a firm can be made liable for malicious prosecution started by a partner with the knowledge and under the general authority of the firm (s).

As regards (iii), i.e. *misappropriation* by a partner, sec. 27 provides that (a) where a partner acting within his apparent authority receives money or other property from a third person, and mis-applies it, and (b) where a firm, in the course of its business, receives money or property from a third person and the same is misapplied by a partner, while in the custody of the firm, the firm is liable to make good the loss.

The important point to remember in the first case is that the moneys must have been received by a partner, while acting within his apparent authority. If he has received otherwise, the firm is not liable. It is a question dependent on the facts of each case whether a partner in the first case received the moneys in course of his authority.

Thus when a partner in a solicitor's firm receives money from a client to be invested in a particular security and thereafter misappropriates it, the

(r) *Kendall v. Hamilton*, 4 App. C. 504.

(s) *Citizen Life Ins. Co. v. Brown* (1904), A.C. 423.

firm is liable to make good the loss (t). On the other hand, receipt of money from a client by a solicitor partner for the purpose of general investment has been held not to be within the "apparent authority" of the partner (u). Similarly, it is within the general scope of a banker's business to sell securities of his customers and to receive the sale proceeds thereof for them (v), but not to receive moneys from customers for general investment (w). As regards the second class of cases, the funds must be within the custody of the firm. If they are within the custody of a partner and are then misappropriated, the firm will not be liable.

Partnership by holding out. (sec. 28)

The sec. deals with the case of a "partnership by holding out", or as it is also called a "*partnership by estoppel*". Where a person (i) represents himself or (ii) knowingly permits himself to be represented as a partner in a firm (when he is in fact not such), he is liable as a partner in the firm, to any one who, on the faith of such representation, has given credit to the firm. Such representation may be made orally or in writing or by conduct. Further, it is not necessary that the person representing or allowing himself to be represented as a partner, knows that the representation has reached the person so giving credit.

The principle of the rule is the same as that underlying all cases of estoppel by conduct for which provision is made by sec. 115 of the Evidence Act. It is based on Equity, viz. that the person who by his representation has induced another person to alter his position to his disadvantage, cannot afterwards be allowed to deny the truth of those representations as against such person. Under the rule, a person may be held liable as a partner with another, although there is in fact no partnership between them. The essential thing is that the third person should have given credit to the firm, on the faith of such representations. Whether such credit has been given, is in all cases, a question of fact.

Notice that the rule of estoppel does not extend to torts (x). It extends however in insolvency (y). A retired partner, who allows his name to remain part of the firm name, may become liable as partner by holding out, if due notice of retirement, as provided by sec. 32, is not given. Notice however that as cl. (2) of sec. 28 itself provides, the rule of estoppel cannot apply where a partner dies and his name is still continued as part of the firm name. This is because there can be no estoppel in death.

The liability of a partner by holding out is a separate liability. Thus a retired partner, who is sued as a partner by holding out, because he has not given the required notice of retirement, is not a joint debtor with his ex-partners. The creditor can sue members of the old or the new firm but he cannot sue them both (z).

Rights of transferee of a partner's share (sec. 29)

A share in a partnership is transferable like any other property, but as the partnership relation is based on mutual confidence, the assignee of a

(t) Blair v. Bromley (1847), 2 Ph. 354.

(u) Harman v. Johnson (1853), 2 E. & B. 61.

(v) Marsh v. Keating (1834), 2 Cl. & F. 250.

(w) Bishop v. Countess of Jersey (1854), 2 Drew. 143.

(x) Smith v. Bailey (1891), 2 Q.B. 403.

(y) Re Rowland & Cranckshaw (1866), L.R. 1 Ch. 421.

(z) Scarf v. Jardine (1882), 7 App. C. 345.

partner's interest, by sale, mortgage or otherwise, cannot enjoy the same rights and privileges as the original partner. Such transferee's rights are defined by sec. 29 as follows: (i) during the continuance of the partnership, such transferee is not entitled (a) to interfere in the conduct of the business; (b) to require accounts or (c) to inspect the books of the firm. (d) He is only entitled to receive the share of the profits of the transferring partner and (e) he is bound to accept the account of profits as agreed to by the partners. Further, (ii) on a dissolution, or on the retirement of the transferring partner, the transferee will be entitled, as against the remaining partners, (a) to receive the share of the assets of the firm to which the transferring partner was entitled to and (b) for the purpose of ascertaining that share, for an account, *as from the date of dissolution* (a).

Notice that even after a dissolution, the transferee's rights to call for accounts is restricted to account for the period after dissolution only. He is not entitled to call for general accounts of the partnership, except in case of fraud. The transferee is not bound by an arbitration clause in the partnership agreement and he can insist on his right for judicial accounts on a dissolution (b). He is also not affected by a settlement of accounts between the partners after the date of the transfer (c).

U Rights and liabilities of minor partner (sec. 30)

Under the well-known ruling of the Privy Council in *Mohari Bibi v. Dharmodas Ghose* (d), it is now settled that a minor cannot be bound by a contract, a minor's contract being void and not merely voidable. A minor, therefore, cannot become a partner in a firm, because partnership is founded on contract. Though a minor, however, cannot be a partner in a firm, he can, as sec. 30 puts it, "be admitted to the benefits of a partnership", i.e. he can be validly given a share in the partnership profits. When this has been done and it can be done only with the consent of all the partners, the rights and liabilities of such minor are defined by sec. 30 as follows:

(i) He has a right to share in the property and profits of the firm, according to his share as agreed upon between the partners.

(ii) He is entitled to have access to, inspect and take copies of the accounts of the firm. Notice that apparently a minor is not entitled to take inspection of or copies of the *books of account* of the firm (see the Report of Select Committee).

(iii) His agreed share in the property and profits of the firm is liable for the acts of the firm, though the minor personally or his personal or separate property is not so liable.

(iv) He has no right while he continues to be a member, to file a suit against the other partners for accounts or for payment of his share in the profits or the property of the firm.

(v) He can only do so, when he wants to sever his connection with the firm.

(vi) In such a suit for severing his connection with the firm, his share will be determined by valuation, according to the principles laid down in sec. 48, for taking accounts of a dissolved partnership.

(a) *Dhanaji v. Gulabchand*, 27 Bom. L.R. 409.

(b) *Bonnin v. Neame* (1910), 1 Ch. 732.

(c) *Veerappa v. Muthiah*, 52 Mad. 509.

(d) 30 I.A. 114.

(vii) In such a suit, however, the other partners, or the partner entitled by agreement to dissolve the partnership by notice, may elect to treat the suit as one for a general dissolution and in such a case, the minor's share shall be determined in the same manner as the shares of the partners are determined on taking general partnership accounts.

(viii) Within 6 months of his attaining majority or of his knowing that he has been admitted into the partnership, whichever is later, the minor must give public notice, as defined by sec. 72, notifying whether he has elected to become or not to become a partner. If he fails to give such notice, he shall be deemed to have elected to become a partner. Further, if the minor relies on absence of knowledge of his being a partner till after 6 months of his majority, the burden of proving such fact is on the minor. Public notice here means a notice to the Registrar, in case of a registered firm, a notice in the local Official Gazette and in one vernacular newspaper circulating in the district where the principal office of the firm is situate (sec. 72).

(ix) Where the minor elects to become a partner (a) his rights and liabilities as between the partners continue the same till such date, but (b) as regards third persons, he becomes *liable for all acts of the firm, from the time he was admitted into the partnership* (and not only from the date he attained his majority or made his election) and (c) his share in the profits and property of the firm shall remain the same, as it was, when he was a minor.

(x) If the minor elects not to become a partner, (a) his rights and liabilities, as between the partners, shall continue the same as before till the date of notice; (b) his share shall not be liable for acts of the firm after date of the notice; and (c) he will be entitled to sue his partners for accounts and for payment of his share as mentioned above.

Legal consequences of partner coming in and going out (secs. 31-38)

These secs. deal with the legal consequences which follow from the coming in of a new partner or the going out of an old partner.

Introduction of a new partner (sec. 31): Under the sec., subject to contract between the partners, no new partner can be introduced into a firm, without the consent of all the existing partners. Of course, if the partnership articles give a right to a partner to introduce a new partner, it will be otherwise. It has been held that an introduction of a new partner under such circumstances will be enforced by the Court by way of specific performance (e). A partner newly introduced, will not be liable for the acts of the firm, done before his entry, unless otherwise agreed.

Retirement of a partner (sec. 32): Under the sec., a partner may retire (i) with the consent of all the partners^(e); (ii) by virtue of an express agreement between the partners; and (iii) in case of a partnership at will, by giving notice *in writing* to all other partners of his intention to retire. Such a partner, however, continues to be liable to third parties for acts of the firm, after his retirement, until public notice of his retirement as required by sec. 72 has been given, either by himself or by the other partners (cls. 3 and 4).

(e) *Byrne v. Reid* (1902), 2 Ch. 735.

As regards liability for acts of the firm done before retirement, the retiring partner remains liable for the same, unless, as cl. (2) provides, an agreement is made by him with the third parties concerned and the partners of the reconstituted firm, discharging him from such liability. Such agreement may be either express or may be implied by a course of dealing between the third parties and the new firm, after knowledge of his retirement. This refers to the subject of "novation" for which see sec. 62 of the Contract Act. Notice that retirement is not the same as dissolution. On retirement of a partner, the firm continues to exist as such, which is not the case when a partnership is dissolved.

Expulsion of partner (sec. 33): The sec. lays down that unless the partnership deed gives a power to do so, a partner cannot be expelled from the partnership, by any majority of the partners. Even when such a power is given, it must be exercised in good faith, i.e. honestly, for the benefit of the firm, in order to be effective in law. If a partner is otherwise expelled, the expulsion is null and void and the "expelled" partner continues to be a partner of the firm and as such, entitled to all the rights of a partner, including his right to a share of the profits of the firm, during the period of "expulsion". The only remedy, when a partner misconducts in the business of the partnership, is to seek judicial dissolution.

Insolvency of partner (sec. 34): The sec. provides that when a partner in a firm is adjudicated insolvent, he ceases to be a partner from the date the order of adjudication is made, and his estate (which thereupon vests in the Official Assignee) ceases to be liable for any act of the firm done after the date of the order. Similarly, the firm also is not liable for any act of such a partner, after such date. On the question whether the partnership is dissolved by the insolvency of a partner, the sec. seems to indicate that it does, for cl. (2) states "where under a contract between the partners, the firm is not dissolved by the adjudication of a partner". See also seq. This is an innovation. Under the old law, insolvency of a partner was merely a ground for dissolving the partnership.

Effect of death of partner (sec. 35): As in the case of insolvency, the present sec. provides that on the death of a partner, his estate ceases to be liable for the acts of the firm, done after such date, if under the terms of the partnership agreement, death does not dissolve the partnership. Thus in *Clayton's case* (f), A who was a partner in a firm of bankers, died but the firm continued the business thereafter. The firm afterwards became insolvent. It was held that A's estate was liable to the customers of the firm for the amounts due to them at the time of his death, so far as they remained due and payable and for all other partnership liabilities upto the said date, but not for debts and liabilities incurred thereafter.

Rights of outgoing partner (secs. 36-37)

The first of these secs. deals with the question of the retiring partner's right to carry on similar business. The second sec. deals with the method of making up accounts, when a partner retires.

Sec. 36 provides that a retiring partner can, (i) carry on similar business with that of the old firm; (ii) he may also compete in such business with the old firm; (iii) he can also advertise such business, but unless the con-

tract otherwise provides, he cannot (a) use the old firm name, (b) represent himself as carrying on the business of the old firm and (c) he cannot solicit customers of the old firm.

As regards carrying on similar business, the sec. provides that a partner, when going out, may agree with his partners that he will not carry on a similar business and if such restriction is reasonable as regards space as well as time, the agreement will be valid, notwithstanding sec. 27 of the Contract Act (dealing with agreements in restraint of trade). The sec. regards an outgoing partner as having sold his share of the goodwill of the firm to the remaining partners, and the sec. attempts to lay down the well-known implications of the sale of goodwill (see sec. 55 seq.).

As regards the method of making up accounts, sec. 37 provides that when a partner dies or retires and the firm carries on business with the property of the firm, without final settlement of accounts between themselves and the outgoing partner or his estate, then, in absence of a contract to the contrary, the outgoing partner or his estate, is entitled to (i) such share of the profits of the firm, made after he ceased to be a partner, as may be attributable to the use of his share in the property of the firm, or (ii) interest at 6 per cent on the amount of his share in the property of the firm. (iii) If the partnership articles provide for the buying up of an outgoing partner's share, and that option is exercised, the rules laid down above will not apply, but they will apply, if after exercise of the option, the other partners do not comply properly with the terms thereof.

The contingency for which provision is made by sec. 37 frequently occurs in practice, e.g. where a partner dies, and the other partners carry on business, without immediately making up the accounts. In such a case, the deceased partner's share in the partnership assets remains with the other partners and, therefore, they are accountable to the estate of the deceased partner, for all profits made by them by the use of such share. What such profits are in a particular case, is a question of fact. They need not bear the same proportion as the deceased partner's share in the partnership (g).

Dissolution of partnership (secs. 39-44)

The group of secs. lay down the law as regards the various ways in which a partnership may be dissolved. A partnership may be dissolved in any one of five different ways :

- (i) by mutual consent ;
- (ii) by notice of dissolution ;
- (iii) by operation of law ;
- (iv) by the happening of certain contingencies ; and
- (v) by a decree of the Court. Dissolution of partnership between all the partners is called the dissolution of the firm (sec. 39).

(i) As regards the first of the above cases, sec. 40 provides that a partnership may be dissolved with the consent of all the partners or in accordance with the contract between the partners. The last apparently relates to cases where partnership articles contain clauses conferring a power of dissolution on certain partners, in certain events, i.e. if they are

not satisfied with the conduct of the other partners. Such options to dissolve, when given, must be *bona fide* exercised and the Court is entitled to investigate whether a purported exercise of such discretion falls within the terms of the particular clauses (h).

(ii) Sec. 43 provides for dissolution of partnership at will. According to the sec., such a partnership is dissolved by any partner giving *notice in writing* to the other partners of his intention to dissolve the firm. The dissolution is complete as from the date of communication of the notice to the other partners. Notice required by the sec. must clearly state an intention to dissolve the firm and must be in writing. A mere record of resolution by a majority of a particular body does not serve as a notice (i).

As regards (iii), sec. 41 provides that a firm is dissolved (a) by the adjudication of all or all but one of the partners as insolvent; (b) by the happening of an event which makes the carrying on of the partnership business or the continued existence of the partnership, unlawful. The fact that one separate adventure or undertaking of a partnership becomes unlawful, will not put an end to the whole firm. Cl. (a) above refers to cases where, as during the last world war, a ban is placed by Government on certain classes of business. In such a case, a partnership for carrying on such business, is automatically dissolved. The cl. also covers cases of partnership between persons, some of whom became alien enemies, by a subsequent declaration of war. In such a case, the partnership is dissolved, because trading with an alien enemy is against public policy. Notice that an alien enemy includes a person of any nationality voluntarily residing in an enemy country (j). It has been held that a partner continuing the business of the firm which is dissolved because the other partner becomes an alien enemy, is bound to account for the profits made by continued use of the other partners' share after dissolution (k). Notice that in the cases contemplated by sec. 41, the partnership is dissolved automatically.

(iv) Sec. 42 deals with what has been called "*optional dissolution*". It provides for cases in which a partnership will stand dissolved, on any of the events mentioned therein happening, unless the contract between the partners otherwise provides. According to the sec., *subject to the contract between the partners*, a partnership is dissolved (a) on the expiry of the term, if constituted for a fixed term; (b) on the completion of the adventure or adventures, if formed for such purposes; (c) by the death of a partner; (d) by a partner being adjudicated insolvent. In any of the above cases, however, the partnership may continue in spite of the provisions of the sec., if the partnership agreement so provides.

Dissolution by Court

(v) Sec. 44 provides for cases where, there being no possibility of a dissolution either by mutual consent, or under any of the provisions of the previous secs., recourse has to be had to a Court of Law for dissolving the partnership. The Court cannot dissolve a partnership for a fixed term at the mere wish of a partner or partners; for that would be sanctioning a breach of contract. The sec., however, gives jurisdiction to the Court to do so, in cer-

(h) Clifford v. Timms (1908), A.C. 12.

(i) Dhulia Amalner M.T. Ltd. v. Raychand, 54 Bom. L.R. 294.

(j) Porter v. Fruendenberg etc. (1915), 1 K.B. 857.

(k) Stevenson v. Cartonnagen etc. (1918), A.C. 239.

tain cases, if certain conditions are fulfilled. According to the sec., the Court may dissolve a firm at the suit of a partner, in the following cases :—

(a) If a partner has become of unsound mind. The application in such a case may be made by any of the other partners or by the next friend of the insane partner.

(b) If a partner has become permanently incapable of performing his duties as a partner, e.g. by a stroke of paralysis. If the disability is temporary, the cl. will not apply. Permanently going out of jurisdiction, would probably be within the cl. The application in such a case may be made by any of the other partners, and not by the incapable partner.

(c) If a partner has been guilty of conduct likely to affect prejudicially the carrying on of the business of the firm; the suit, in such a case can only be brought by the other partners. It is difficult to state categorically what conduct would fall within the terms of the cl. It depends upon the nature of the business of the firm, as the cl. itself says. Thus the conviction of a partner for adultery, in a case where the firm was carrying on mercantile business, was held not to justify a judicial dissolution (l). On the other hand, in case of a firm of obstetricians, it was held to be enough (m). Misappropriation of partnership funds (n) or moneys belonging to a customer of the firm would be obviously covered.

(d) If a partner wilfully or persistently commits breach of the agreement with regard to the management of or the conduct of the business of the firm or otherwise so conducts himself in the business of the firm as not to make it practicable for other partners to carry on the partnership business with him, the Court can dissolve the partnership. Under this cl., the fact of continued hostility between the partners, which makes co-operation between them impossible (o), the fact of one partner habitually charging the other with gross misconduct in the business of the firm (p), have been held to be sufficient reasons. Similarly, continuous refusal by a partner to attend to his duties in the partnership business has also been held enough (q). Only partners other than the guilty partner can, in such a case, move the Court for dissolution.

(e) If a partner transfers in any way (e.g. by mortgage, charge, sale or otherwise), his whole interest in the partnership to a third party, or allows his share to be charged in execution of a decree against him (under O. 21, r. 49, of the Civil Procedure Code), or allows the same to be sold for arrears of land revenue or for charges recoverable as land revenue, the Court can dissolve the partnership. The suit in such a case has to be brought by any other than such partner.

(f) The Court can also dissolve the partnership, if the business of the firm cannot be carried on save at a loss. Thus if the purposes of the firm cannot be carried into effect with any reasonable prospect of profit, the Court will generally dissolve the partnership.

(g) The Court can also dissolve the partnership, for any other ground which renders it just and equitable that the firm should be dissolved. The last cl. gives the discretion to the Court as regards dissolution of partnership.

(l) *Snow v. Milford* (1868), 18 L.T. 142.

(m) *Anon* (1856), 2 K. & J. 441.

(n) *Cheeseman v. Price*, 35 Beav. 142.

(o) *Baxter v. West*, 127 R.R. 64.

(p) *Watney v. Wells*, 30 Beav. 56.

(q) *Krishnamacharya v. Sankar*, 22 Bom. L.R. 1343.

The Court however cannot dissolve a partnership on the mere ground that in its opinion, it would be, on the whole, the best course.

Consequences following dissolution of a firm (secs. 45-55)

These secs. deal with the various consequences which follow upon the dissolution of a firm. The important questions considered are: (i) rights of partners after dissolution (sec. 46-7), (2) method of settling partnership accounts (sec. 48), (3) discharge of partnership debts (sec. 49) and (4) rules as regards sale of goodwill (sec. 55).

Continuing liability of partners after dissolution (sec. 45): Sec. 45 provides that notwithstanding the dissolution of a firm, the partners remain liable as such to third parties for the acts of any one of themselves, which if done before dissolution would have been an act of the firm, till public notice of dissolution as required by sec. 72 is given. Notice here referred to is notice to the Registrar, in case of registered firms, notice in the local official Gazette and in one vernacular newspaper circulating in the district where the firm's principal place of business is situate. It can be given by any of the partners. The sec. in effect provides that the dissolution of a firm, as regards third parties, is not complete till public notice is given thereof as mentioned above; till then, all partners remain liable as partners to outsiders for any act of the partner, if done by him in the usual course of his authority as partner.

Three exceptions to the rule are laid down by the proviso: (i) in case of death or (ii) insolvency of a partner and (iii) in case of a retiring partner, who is not known to the person dealing with the firm to be a partner. The last refers to what is called a "*dormant partner*", i.e. a partner whose existence as such is not known to the outside world. To these three cases, the continued authority of a partner to bind the partnership, after dissolution, by his acts, which is laid by the sec., does not extend. Thus, under the sec., a firm, though dissolved, becomes liable on a bill of exchange drawn, endorsed or accepted by one of its partners in the partnership name after dissolution, if the person taking such bill was unaware of the dissolution and if no public notice of the same had been given (r), provided such dealing with the bill was within the ordinary competence of the partner before dissolution. Under the old law, it was held by the Privy Council (s) that old customers of the firm required special notice over and above the public notice provided by law. This distinction between different classes of customers, however, does not hold good now.

Right to enforce winding up (sec. 46): The above sec. lays down that on a partnership being dissolved, any partner or his representative has a right, against the other partners, to have (i) the property of the firm applied in payment of the debts of the firm and (ii) to have the surplus distributed amongst the partners or their representatives according to these respective rights.

The sec. gives to each partner, a right to have the partnership affairs wound up and the partnership accounts taken by and under the directions of the Court, in case the partners fail to reach an agreement as regards winding up. It creates an *equitable lien*, which is available to a partner or his legal representatives against the other partner and all persons claiming

(r) *Exparte Robinson*, 3 D. & Ch. 388.

(s) *Jwala Dutt v. Bansilal Motilal*, 56 I.A. 174.

under him, e.g. an official assignee of the estate of such partner. Notice that while a partnership is functioning, no suit lies at the instance of a partner to take partnership accounts merely, without asking for a dissolution (t). Special grounds must be made out for justifying such a suit, e.g. that a partner is trying to exclude a partner from the partnership for some secret benefit or to force him to a dissolution; that there is a refusal to account or where a limited account will meet with the justice of the case (Halsbury, Vol. 22, p. 71). Further, partners are not, as regards partnership dealings, considered debtor and creditor *inter se* until the final settlement of accounts between them on a winding up. A partner, therefore, cannot sue the other partners for moneys lent by him to the firm, because such advance is merely an item in the partnership account (u). If the loan, however, is a separate and distinct transaction, e.g. where the loan is to a partner for making up his capital contribution, or where the moneys are advanced to the firm and a promissory note is signed by the other partners in respect thereof, a suit to recover the loan is maintainable, without asking for general accounts (v). A suit on a promissory note passed by one partner to another on adjustment of partnership account can be filed, without bringing a suit for general account of the partnership (w). No suit can lie between two firms with a common partner with regard to a transaction between them, because in such a case a person will be both plaintiff and defendant (x). The Court, in case of a dissolved partnership, generally appoints a receiver of the partnership assets, pending the taking of the partnership accounts and the actual distribution of the shares (y). It is otherwise, where the partnership is not dissolved. In such cases, fraud or wilful misconduct or other prejudice to the partner's interests must be shown, before a receiver can be appointed (z).

The limitation period for accounts of a dissolved partnership and for payment of one's share is 3 years from the date of dissolution under Art. 106 of the Limitation Act.

Partners' continuing authority after dissolution (sec. 47): As the above sec. lays down, the authority of a partner and the mutual rights and obligations of partners continue after the dissolution only for (i) winding up the affairs of the firm and (ii) for completing transactions pending at the date of dissolution and no more. In other words, a partner's authority as agent of the firm terminates on dissolution.

An *exception* is recognised only in the above two cases. Thus a sale by a partner of partnership property in the course of winding up, will be binding on the other partners, though the firm is dissolved. Similarly, moneys borrowed by a partner in a dissolved firm to complete a pending contract of the firm, will be binding on the other partners, though no express authority is proved. The partners, however, are not bound by such acts of a partner, if he is adjudicated insolvent, unless they have held him out as a partner.

(t) *Mistry v. N. H. Moos*, 10 Pat. 792.

(u) *Rustomji v. Sheth Parshotamdas*, 25 Bom. 606.

(v) *Vallam v. Mallupeddi*, 31 Mad. 343.

(w) *Chhaganlal v. Jagjivandas*, 41 Bom. L.R. 1263.

(x) *Rustomji v. Seth Parshotamdas*, *supra*.

(y) *Pini v. Roncoroni* (1892), 1 Ch. 633.

(z) *Evans v. Coventry*, 5 D.M. & G. 911.

Settlement of partnership accounts (sec. 48)

The sec. lays down the law as regards the manner in which partnership accounts are to be taken on a dissolution of a firm. The sec. says : subject to any agreement between partners, in taking partnership accounts,

(i) Losses, including losses on capital, must be paid, first from profits, next out of capital and lastly, if necessary, by contribution of each partner in proportion to his share in profits.

(ii) The assets of the firm, including sums contributed by partners to make up deficiency of capital, shall be applied : (a) in paying debts of the firm to outsiders ; (b) in paying each partner rateably, for advances made by him to the firm as distinct from capital ; (c) in paying each partner rateably, amount due for capital contribution ; and (d) the residue in paying each partner in accordance with his share in the profits of the firm.

The sec. gives legislative sanction to well-recognised rules of accounting, in case of taking accounts of a dissolved partnership. Notice that losses are *prima facie* to be borne equally. Where profits are not equally divided losses also are to be divided in the same proportion. The liability to share losses may be excluded by special agreement. Where the contributions to capital are unequal, and the partners share the profits equally, all the partners are bound to contribute equally, if a deficiency of capital occurs. The assets of the firm will thereafter be applied to pay each partner rateably, what is due to him on account of capital. This is called in accountancy, the rule in *Garner v. Murray* (a). Notice that a partner's share is in substance, that which comes to the share of a partner after all the debts of the firm have been paid off and after accounts are finally taken. It is therefore not tangible property. As the Privy Council put it (b), it is no more than "a right to participate in the profits of the firm, after its obligations have been satisfied".

Rules as regards payment of partnership debts (sec. 49)

The above sec. lays down a rule as regards administration of partnership assets on a dissolution. According to the sec., where there are joint debts due from the firm and also separate debts due from any partner, (i) the property of the firm shall be first applied in payment of the partnership debts ; if there is any surplus, the share of each partner therein, shall be applied in payment of his separate debts. (ii) The separate property of each partner shall be applied, in the first instance, in payment of his separate debts and the surplus (if any), in payment of the debt of the firm.

The sec. lays down the well-known rule laid down in *Lodge v. Prichard* (c) which relates to administration of partnership assets in bankruptcy and applies it to the case of every dissolved partnership. According to the sec., where two kinds of debts co-exist, e.g. partnership debts and separate debts of each partner, the partnership property must be first applied in payment of partnership debts and the separate property of each partner in payment of his separate debts, and it is only the surplus (if any) in each case, which can be used in payment of the debts of the other kind. The rule as laid down by the sec. gives to each partner what is called an

(a) (1904), 1 Ch. 57.

(b) Sanyasi Charan v. Krishnadhan, 49

L.A. 108.

(c) (1863), 1 De. G. & J. & S. 610.

"*equitable lien*", which can be enforced against the other partners, e.g. by a retiring partner against a continuing partner. Of course, creditors are not affected by the rule. Separate creditors of a partner have as much right to proceed against his share in the partnership as they have against his separate estate. If the partnership is insolvent, however, creditors (whether joint or separate), are bound by the above rule.

Personal profits after dissolution (secs. 50 and 53)

The first sec. provides that where a firm is dissolved by the death of a partner and the surviving partner or the representative of the deceased partner carries on the business of the firm, any personal profits made by them by such means, before the firm is fully wound up, must be accounted for by them to the other partner's estate. Thus a lease expiring on the death of a partner, which is renewed by the surviving partner before final winding up, belongs to the partnership (d).

The sec. has to be read with sec. 53, which provides that in absence of an agreement to the contrary, each partner or his representative is entitled to restrain (by injunction) the other partners from carrying on a similar business in the name of the firm or from using the property of the firm for their own benefit till the affairs of the firm are completely wound up. Exception is only made in case of a partner who has bought the goodwill of the firm; such a partner can carry on business in the firm name.

Return of Premium (sec. 51): Sometimes, a partner having been newly introduced into a firm, on his paying a certain sum by way of premium, the partnership is dissolved before its due date, by insolvency of a partner or otherwise. In such cases, the sec. provides that the partner so introduced will be entitled to be repaid the whole or a reasonable part of the premium, the amount to be determined by having regard to the terms on which he was admitted and the length of time during which he was a partner.

The rule does not apply if (i) dissolution is caused by death of a partner, (ii) if dissolution is caused by the misconduct of the partner so admitted, or (iii) if dissolution is due to an agreement containing no provision for return of premium. The general rule is that except in the three above cases, proportionate premium will always be ordered to be refunded, where a partnership is dissolved before its appointed time (e).

Rescission of partnership agreement on ground of fraud, etc. (sec. 52): A partnership agreement is a contract based on utmost confidence. No fraud or misrepresentation should be practised by one partner on the other in bringing it about. If such is the case, the partner misled will be entitled to rescind the agreement, and will, in addition to his other rights, have the following further rights, as laid down by the sec.: (i) a lien on the surplus assets of the firm for purchase price paid by him for his share and for his capital contribution to the firm; (ii) to rank as a creditor of the firm, as regards any debts of the firm paid by him; (iii) to an indemnity from the partners guilty of such fraud or misrepresentation against the debts of the firm.

Agreement in restraint of trade (sec. 54): The above sec. provides that partners in anticipation of or upon dissolution of the firm, can agree that all

(d) *Clement v. Hall*, 2 De. G. & J. 173.

(e) *Atwood v. Maud*, L.R. 3 Ch. 369.

or some of them will not carry on a business similar to the old one, for a certain specified time or within certain specified limits. If the restrictions are reasonable, they will be valid, notwithstanding sec. 27 of the Contract Act.

Goodwill on dissolution (sec. 55)

"Goodwill" is a commercial rather than a legal term and it is difficult to define it with exactitude. It has been described by Lindley as "the benefit arising from connection and reputation".

What the purchaser of a "goodwill" acquires is: (i) the right to carry on the same business under the old name, and (ii) to represent himself to the customers of the old firm as the successor in business of the old firm. The sec. lays down that subject to the contract between the partners, "goodwill" of a firm is to be included in the assets of the firm on dissolution and that on such dissolution, the goodwill can be sold, at the instance of any partner, either separately or along with the other assets of the firm.

Cl. (2) of the sec. defines the rights of partners selling the goodwill of a firm on dissolution, as against the purchaser thereof. Under the sec., such partners (i) can carry on a similar business; (ii) can also compete with the business sold by them to the purchaser; and (iii) can also advertise their business in such manner as they deem fit, but, subject to an agreement to the contrary, they cannot, (i) use the firm name; (ii) represent themselves as carrying on the old business; and (iii) cannot solicit the customers of the old firm. (iv) A partner on selling "goodwill" may agree with the buyer that he will not carry on similar business within certain specified limits and for a certain specified time and if such restrictions are reasonable, they will be valid, notwithstanding sec. 27 of the Contract Act (restraint of trade).

The first three rules were laid down by the House of Lords in *Treggo v. Hunt* (f). The restrictions mentioned therein apply to the executor of the seller of goodwill also (g). Where a firm is dissolved without making any provision as to goodwill, the rule is that each partner may carry on the same business in the old firm name, provided he does not, by so doing, expose the other partners to the risk of being partners by holding out (h). Where the goodwill of the business is transferred involuntarily, e.g. by sale in bankruptcy, the purchaser cannot restrain the bankrupt from canvassing old customers (i).

Registration of partnerships (secs. 56-71)

Chapter VII of the Partnership Act dealing with registration of firms is new. It contains provisions for voluntary registration of firms. Sec. 56 gives power to the Central Government to declare the Chapter not applicable to any province or a part thereof. The Local Government is given power to appoint Registrar of Firms for particular areas, who are to be regarded as Public servants (sec. 57). The Central Government is given power to prescribe the fees to be paid with regard to any document which is sought to be registered, while the Local Government is given the power to frame rules for the working out of the details of the provisions of the Chapter (sec. 71).

(f) (1896), A.C. 7.

(g) *Boorne v. Wicker* (1927), 1 Ch. 667.

(h) *Burchell v. Wilde* (1900), 1 Ch. 551.

(i) *Walker v. Mottram* (1881), 19 Ch.D. 355.

Registration of firms (secs. 58-59): The first sec. provides that registration of a firm may be affected at any time, (i) by sending to the proper Registrar a statement (in prescribed form and with prescribed fee) containing (a) the firm name; (b) the principal place of business of the firm; (c) names of its other places of business; (d) the date of each partner joining; (e) the name and full permanent addresses of all partners and the duration of the firm. The statement must be signed by all partners or their recognised agent. It shall also be verified by such persons.

The *firm name* must not contain words like, 'Crown', 'Emperor', 'Royal' or others, showing Royal patronage, unless written sanction of the Central Government has been obtained. Sec. 59 provides that the Registrar shall on receipt of the statement, make an entry of such statement in the Register of Firms and shall also file it. Notice that, as sec. 58 provides, the registration "may" be effected "*at any time*". Thus there is no time-limit fixed for registration. It may be effected even after dissolution.

Registration of subsequent alterations in a firm (secs. 60-68): The above secs. provide for registering various alterations which may occur during the continuance of the firm. Thus under sec. 60, where the firm name or the principal place of business of the firm is altered, the said facts may be registered by the Registrar on a properly signed and certified statement being filed with him by a partner or partners; similarly, where an old place of business is closed or a new place of business is opened (sec. 61), or there is a change in the names and addresses of partners (sec. 62). Where a change in the constitution of the firm occurs or the firm is dissolved, sec. 63 provides that any partner or a specially authorised person on his behalf may give notice of the fact to the Registrar with the date thereof. The Registrar shall record the notice in the Register of Firms and shall also file the notice with the other papers, filed under sec. 59.

Similarly, when a minor elects to become or not to become a partner on attaining majority, he or his authorised agent may give notice to the Registrar of such election and the Registrar shall note the same as above. Sec. 64 gives power to the Registrar to rectify errors in entries made by him with regard to documents filed with him under the above secs., on application of all parties concerned with such documents.

Under sec. 65, the Registrar can rectify the Register so as to make it accord with the orders of any Court. The Register of Firms, under sec. 66, is to be open to all persons for inspection on payment of the prescribed fees, while under sec. 67, certified copies of all documents filed with the Registrar can also be had.

Sec. 68 lays down an important *rule of evidence*. It provides that any statement, intimation or notice recorded or noted in the Register of Firms, shall, as against all persons signing the same, be *conclusive proof* of all facts stated therein. Further, a certified copy of an entry in the Register of Firms may be produced as proof of the statements therein recorded. Under sec. 70, persons furnishing false particulars to the Registrar are penalised. Sec. 71 gives powers to the Central Government and Local Governments to make proper rules for carrying out the above provisions.

Consequences of non-registration (sec. 69): This is the most important provision in the whole of this Chapter. It lays down the legal consequences which will follow, on account of non-registration of a firm.

The sec. provides that (i) no partner or alleged partner, can file a suit to enforce a right arising from a contract or conferred by the Act, against the other partners or alleged partners or the firm, unless the firm is registered as required by the Act and the person is shown as a partner in the Register of Firms. Notice that this only requires registration before filing the suit. Further, registration is a condition precedent to the filing of a suit. A suit filed without such previous registration will therefore be dismissed. Registration cannot be effected after suit. A suit falling under sec. 69 which has been filed by a partnership without registration must be dismissed (j). Registration is necessary in cases of suits arising from contract or in respect of a right conferred by the Act. Thus no registration is necessary where the suit is in respect of a "tort" committed by a partner. A dissolved partnership can file suit for recovering damages for a breach of contract though not registered (k). 'Contract' would probably refer to the partnership articles, while rights conferred by the Act would be the rights of management, inspection, accounts and such others.

(ii) Further, no suit can be filed by a firm against third parties to enforce a right arising from a contract, unless the firm is registered and the persons suing are shown as partners therein in the Register of Firms. Notice that this refers to suits by firms against third parties in respect of contracts, e.g. to recover a debt, to enforce a promissory note, to recover damages for a breach of contract. Suits in respect of torts are outside the sec. The above provisions are also applicable to claims for set-off made by or on behalf of the firm.

There are however certain *exceptions* to these rules. The above rules do not apply: (1) to a suit for dissolution of a firm; (2) for accounts of a dissolved firm; (3) for realisation of the property of a dissolved firm; (4) to the power of the Official Assignee or a Receiver of the estate of an insolvent partner to realise the property of the insolvent; (5) to firms which have no place of business in India, i.e. foreign firms; and (6) to suits or claims for set-off, not exceeding Rs. 100 in value, which according to law, have to be filed in the Small Causes Court, and to proceedings incidental to such suits. In other words, in such cases, a suit can be filed, although the firm is not registered. It has been held in Madras that under sec. 69(3), a partner of a dissolved firm can sue to recover a debt due to the firm which on dissolution has come to his share though the firm is unregistered (l). A dissolved partnership can file suit for recovering damages for a breach of contract, though not registered (11). It has been held in Calcutta that the fact that a partnership is not registered, does not prevent the partnership from referring a dispute to arbitration (12). Similarly non-registration is no bar to setting up a partnership property claim, by way of defence (13).

(j) Prithvising v. Haji Hasanali, 52 Bom. L.R. 862; Govindmal v. Kunj Biharlal, 56 Bom. L.R. 348; Dwijendranath v. Chandra, A.I.R. (1953) Cal. 497.
(k) Bhagwanji v. Alembic Chemical Works, 45 Bom. L.R. 691; Abdul Karim v. Ramdas, A.I.R. (1951), Nag. 159.

(l) Punnaiyya v. Battu, A.I.R. (1948), Mad. 441.

(11) Bhagwanji v. Alembic Chemical Works, 45 Bom. L.R. 691.

(12) Meghraj v. Raghunath, A.I.R. (1955) Cal. 278.

(13) Ajit Kumar v. Narendra, 59 Cal. W.N. 136.

CHAPTER XII

NEGOTIABLE INSTRUMENTS

Negotiable Instrument : What is

No satisfactory definition of a "negotiable instrument" is available, though there have been many attempts by various authors to do so. The "Negotiable Instruments Act" defines a negotiable instrument as meaning "a promissory note, bill of exchange or cheque, payable either to order or bearer" (sec. 13). This, however, can hardly be called a definition. Perhaps the best available definition is the one given by Thomas in his "Principles of Banking". It is as follows: "A negotiable instrument is one which is, by a legally recognised custom of trade or law, transferable by delivery or by endorsement and delivery in such circumstances that (a) the holder of it for the time being may sue on it in his own name and (b) the property in it passes, free from equities, to a *bona fide* transferee for value, notwithstanding any defect in the title of the transferor."

Special characteristics of a negotiable instrument

As can be gathered from the above definition, nego. insts. have the following special characteristics :

(i) They are transferable from hand to hand like cash, in other words, the property in these instruments passes by either endorsement and delivery or by delivery merely.

(ii) The transferee of a nego. inst. is entitled by law to sue on the instrument in his own name in case of dishonour. This special characteristic of a nego. inst. distinguishes it from a transfer or "assignment" of, what, in the law of property is called, an "actionable claim". A nego. inst., e.g. a cheque, represents a debt. On its being negotiated by indorsement and/or delivery, what is transferred is a debt, i.e. an "actionable claim" (called in English law, with a slight difference, a "chose in action"). Under the Common Law of England, and under Indian Law also, before the Transfer of Property Act, a transferee of an "actionable claim" had no right to sue in his own name but had always to join his transferor, i.e. the original creditor, before he could recover his claim from the debtor. This was a serious difficulty in the way of transfers of "actionable claim". An indorsee of a nego. inst., however, need not join his indorser, before he can recover the amount of the instrument from the party liable. Notice that under the Transfer of Property Act (sec. 130), an assignee of an "actionable claim" is given the right to sue the original debtor in his own name, provided the conditions of the sec. are satisfied.

(iii) A *bona fide* transferee of a nego. inst. for value takes it free from all defects in the title of his transferor. This is the main and the fundamental distinction between a nego. inst. and other subjects of ordinary transfer. The general principle of the law of transfer is that no transferor of goods can give to his transferee a better title to the goods than what he himself has (see ante). To this general rule, nego. insts. are a significant

and important exception. If A is the holder of a bill of exchange payable to bearer, and B obtains it from him by theft, obviously B has no title to the instrument. But if B delivers it over to C who pays value for it and is ignorant of the theft, C obtains a good title to the instrument, as being a "holder in due course" thereof. The result would have been entirely different, if, instead of a bill of exchange, say a watch had thus been transferred.

Examples of negotiable instruments

The following instruments have been recognised as nego. insts. by custom or usage of merchants: (i) bills of exchange; (ii) cheques; (iii) promissory notes; (iv) G. P. Notes (*m*); (v) bank notes (*n*); (vi) Exchequer Bills (*o*); (vii) Bankers' drafts; (viii) dividend warrants (*p*); (ix) share warrants; (x) circular notes (*q*); (xi) bearer debentures (*r*); (xii) treasury bills; (xiii) bearer bonds of various Colonial and Foreign Governments (*s*); (xiv) Hundis. (xv) Recently debentures of the Bombay Port Trust payable to order have been held to be promissory notes and therefore nego. insts. (*t*).

Examples of non-negotiable instruments

These are: (i) money orders and Postal orders; (ii) deposit receipts; (iii) share certificates; (iv) bills of lading (*u*); (v) dock warrants. The last two are called "documents of title" and have some of the special characteristics of a negotiable instrument, e.g. of being capable of being transferred by endorsement and/or delivery but they do not possess the essential qualification of a nego. inst., viz. they do not, on transfer, confer on a *bona fide* transferee for value, a title free from all defects in the title of the transferor. Such instruments are sometimes called "quasi-negotiable instruments".

An "I.O.U." is an instrument given by a debtor to his creditor acknowledging the debt. *Prima facie*, it is merely an acknowledgment of a debt and an evidence of "account stated". The acknowledgment is firstly an admission of the amount due and secondly, an implied promise to pay the amount. The creditor therefore can sue the debtor either on the moneys originally lent and advanced or on the "account stated". An I.O.U. however is not a nego. inst. If therefore the debt represented by the instrument is desired to be transferred by the creditor, he can only do so by a proper assignment under the "Transfer of Property Act" and not by "negotiation". There may however be words added to an "I.O.U." which makes it a nego. inst. Thus when a document ran "I.O.U. £20, to be paid on the 22nd", it was held to be a promissory note (*v*).

It should be noticed that an instrument which is ordinarily "negotiable" can be made "non-negotiable" by using proper terminology, e.g. a bill of

(*m*) *Hansraj v. Ratansi*, 24 Bom. 65.
 (*n*) *Miller v. Race* (1758), 1 Burr. 452.
 (*o*) *Woolley v. Pole* (1820), B. & Ald. 1.
 (*p*) *Webb Hale & Co. v. Alexandria Water Works* (1905), 93 L.T. 339.
 (*q*) *Confians Quarry Co. v. Parker*, L.R. 3 C.P. 1.
 (*r*) *Bechuanaland Exploration Co. v.*

London Trading Bank (1898), 2 Q.B. 658.
 (*s*) See *Chalmers*.
 (*t*) *Mercantile Bank of India v. Mesca-*
renhas, 56 Bom. 1.
 (*u*) *Gurney v. Behrend* (1854), 3 E. & B. 663.
 (*v*) *Brooks v. Elkins* (1836), 2 M. & W. 734.

exchange payable to "X only" is a non-negotiable instrument, because the words of the instrument clearly show an intention against its negotiability. Similarly, a cheque marked "not negotiable," is not a "negotiable instrument" in the true sense of the word, because though it can be transferred by endorsement and/or delivery, it will not confer on its transferee, any better title than the title of its transferor, though the former may have taken the instrument *bona fide* for value, without notice of any defect therein. The above list of nego. insts. is not exhaustive. As implied by the definition of a "negotiable instrument" (see sec. 13 which uses the words "means and includes"), the list is capable of expansion on proof of mercantile usage, which accords the character of a "negotiable instrument" to any particular document.

Negotiability by estoppel

An instrument which is not ordinarily a nego. inst. may be so drafted as to preclude the person who circulates it, from denying that it is a negotiable instrument. Such instruments are called negotiable instruments by estoppel (w).

BILLS OF EXCHANGE

Definition: Barring cheques, the document which is most commonly in use amongst merchants is a bill of exchange. A bill of exchange is defined by sec. 5 as "an instrument in writing, containing an unconditional order, signed by the maker, directing a certain person, to pay certain sum of money, only to or to the order of a certain person, or to the bearer of the instrument".

Special characteristics

An instrument, in order to amount in law to a bill of exchange, must fulfil the following conditions: (i) It must be in writing (ii) signed by the maker; (iii) it must contain an order (iv) which must be unconditional; (v) it must direct a certain person (vi) to pay certain sum of (vii) money only (viii) to a certain person or his order or to bearer. (ix) It must be properly stamped. Briefly speaking, before a document can be called a bill of exchange, the drawer must be certain, the order must be certain, the drawee must be certain, the payee must be certain, and the sum payable must also be certain. These are popularly called the "five certainties" of a bill of exchange.

Special characteristics considered: Taking each of the special characteristics *seriatim*: as to (i) it should be noted that a bill of exchange cannot be oral; it must always take the form of a written document. No particular words are necessary to be used nor is there a set form in which alone a bill of exchange can be drawn. Provided the document fulfils the above conditions laid down by law it will amount to a bill of exchange, whatever its form may be. Writing includes printing.

(ii) A bill which is not signed by the drawer is regarded in law as an "inchoate bill" (see seq.). The signature of the drawer may not be affixed

to the document at the time it is drawn but till this is done, the bill is inchoate and ineffective in law. Thus no action can be brought by a holder against the acceptor on a bill which is unsigned by the drawer (x). Signature includes a mark and even an impressed or litho stamp. The signature on a bill of exchange need not necessarily be of the drawer himself in order to make it valid; the signature of an authorised agent on behalf of the drawer is sufficient for the purpose (see seq.).

(iii) Though no particular form of words is necessary in order to constitute a valid bill, it is essential that the words used must amount to an "order". In other words, they must not be precatory, i.e. amounting to a mere request, which the addressee is at liberty either to carry out or refuse to carry out.

Thus where the words used were "Mr. Little, please to let the bearer have seven pounds and place it to my account and you will oblige, your humble servant R. Slackform", it was held that this was not a valid bill (y). On the other hand, where the words used were "Mr. Nelson will oblige Mr. Webb by paying to J. Ruff, or order twenty guineas on his account", it was held to be a valid bill (z).

(iv) It is of the essence of a bill that the order directing payment should be unconditional, i.e. the payment should not, on the face of the bill, be dependent on the happening of a contingency or the fulfilment of a condition.

Thus an order directing payment to be made "if a certain ship arrives" (a), "on marriage" (b) or "when realised" (c) is not a valid bill of exchange. Similarly, where moneys are directed to be paid out of a certain fund, e.g. out of amount standing to one's credit or "out of moneys coming from X" (d), it has been held that the document is not a valid bill, because there may be no or no sufficient fund or no money may be recovered at all.

A direction to the drawer, however, to reimburse himself out of a particular fund will not make the bill conditional. Further, as the expl. to sec. 5 points out, a bill will not be regarded as conditional, because it makes the payment conditional on the happening of an event, which in the ordinary course of nature must happen, though the exact time of its happening may be uncertain, e.g. "on the death of X".

(v) The drawee must be certain. If the name of the drawee is not mentioned, the bill is incomplete, and nobody who accepts the bill in that condition can be made liable at law as an acceptor. Of course there is nothing to prevent the holder in such a case from treating the bill as a promissory note and treating the "acceptor" as the maker thereof (e). Notice that there can be joint drawees of a bill but not alternate or successive drawees. Further, if the drawee's name is wrongly mentioned, evidence may be led to prove who was the person really intended. In an English case (f) the name of the drawee was omitted but his residential address was mentioned, and the person concerned accepted the bill. It was held that he could be validly held liable as an "acceptor".

(vi) The sum payable must be certain. A direction to pay "£65 and all sums that may be due" does not make a valid bill (g). As the expl. to

(x) *M'call v. Taylor* (1865), 34 L.J. C.P. 365.

(y) *Little v. Slackford* (1828), M. & W. 171.

(z) *Ruff v. Webb* (1794), 1 Esp. 129.

(a) *Palmer v. Pratt* (1824), 2 Bing. 185.

(b) *Pearson v. Garret* (1693), 4 Mod. 242.

(c) *Alexander v. Thomas* (1851), 16 Q.B.

333.

(d) *Dawkes v. De Lorrain* (1770), 3 Wills

207.

(e) *Fielden v. Marshall* (1861), 30 L.J. C.P. 158.

(f) *Gray v. Milne* (1819), Taunt 739.

(g) *Smith v. Nightingale* (1818), Stark 375.

sec. 5 points out, however, the sum is not uncertain because it is directed to be paid with interest, or by instalments or at the prevailing rate of exchange (as in case of a foreign bill).

(vii) The amount directed to be paid must be expressed in terms of money only. Thus an order to pay a certain sum and also to deliver up a horse was held not to be a valid bill (h). Similarly, a direction to pay money and to hand over a security is not a bill (i).

(viii) The bill must be drawn and made payable either to a certain person or his order or to bearer. In this connection it has been recently held in England that a document drawn payable to "Cash or order" is not a bill of exchange as it is not made payable "to or to the order of any specified person or bearer" (j).

The payee must also be certain, i.e. clearly specified on the face of the bill or being otherwise capable of being ascertained with certainty. Notice that it is not necessary for the validity of a bill that the payee must be different from either the drawer or drawee. A bill drawn by A on B in favour of himself is a valid bill; similarly, a bill drawn by A on B in favour of B is also valid. In the last case however the bill is not effective till the drawee endorses it in favour of another. Note further that the Act specifically lays down that a bill may be made payable to joint payees or to payees in the alternative.

(ix) Art. 13 of the Stamp Act lays down the proper stamp for bills of exchange (see seq.). Generally speaking, no stamp is chargeable on a bill payable on demand. As regards other bills, the duty is 2 annas per thousand or a portion thereof, if bill is payable not more than one year after date or sight; in all other cases the same duty as in case of a bond. A bill must be properly stamped when necessary. In absence of a proper stamp, the bill may be inadmissible in evidence (sec. 35, Stamp Act). Notice that under sec. 46, the making (acceptance or indorsement) of a bill of exchange is not completed till delivery thereof, either actual or constructive.

Over and above the above particulars the following points in connection with a bill of exchange may be noted: *Figures*: the bill at the top or the bottom corner mentions the amount in figures. The Act provides that where the sum payable is expressed in words and also in figures and there is a discrepancy between the two, the sum expressed in words is the amount payable (sec. 18). *Date*: the date is mentioned in order to compute maturity of bill. That date is by law regarded as the date of the issue of the bill. A bill is not invalid because it is undated. Evidence may be adduced to prove the date of its issue. A bill may be ante dated or post dated. *Place of issue* is also mentioned. This is to determine whether it is an "inland" or a "foreign" bill. "*For value received*": the words though generally found in bills of exchange are really superfluous, consideration being always presumed in case of negotiable instrument (sec. 118) and also because consideration can always be proved by extrinsic evidence.

PARTIES TO BILLS OF EXCHANGE

Parties to bills of exchange: There are generally three parties to a bill of exchange: (i) *the drawer*, i.e. the person giving the order, (ii) *the drawee*, i.e. the person to whom the order is addressed and (iii) *the payee*, e.g. the person named in the instrument to whom or to whose order the money is directed to be paid (sec. 7). Over and above these parties, however, there

(h) *Martin v. Chantry* (1747), 2 St. 271.
(i) *Follet v. Moore* (1849), 19 L.J. Ex. 6.

(j) *Colc v. Milsom* (1951), 1 All E.R. 318.

may be ~~for~~ parties also to a bill of exchange, e.g. *acceptor* means the drawee of a bill of exchange who (i) has signed his assent upon the bill or any part thereof and (ii) delivered the same or given notice of the same, to the holder or any person on his behalf (sec. 7). Both the above conditions must be fulfilled before a drawee can become liable as an acceptor. Notice that under sec. 33, no person, except the drawee named in the bill or all or several drawees if they are more than one, or a "drawee in case of need" or "an acceptor for honour", can accept a bill. A bill cannot be drawn on two drawees in the alternative or on successive drawees. Under sec. 34, where there are several drawees, each must accept, unless (a) they are partners or (b) one of them is an agent for the others, acting within the scope of his authority. An acceptance by one of several drawees, in other cases, amounts in law to a qualified acceptance and the bill thereby becomes dishonoured (see sec. 86).

Drawee in case of need

Where it is found that the drawee on whom a bill is drawn may not be able or willing to accept or discharge the bill, the drawer generally mentions, on the bill itself, the name of another person to whom recourse may be had for payment, if the drawee dishonours the bill. Such a person is called a "drawee in case of need" or "in case of need" simply (sec. 7). His name may be inserted by any endorser also.

The particular features of such a bill are (i) that the instrument in law is not treated as dishonoured till it is presented to such "drawee" for payment and is dishonoured by him (sec. 115); (ii) it can be presented to the drawee in case of need without being "noted" or "protested" for dishonour.

Acceptor for honour

Where a bill is dishonoured for non-acceptance or non-payment, any person who comes forward and accepts it, "*supra protest*", for saving the honour of any party already liable on the bill, is called an "acceptor for honour" (sec. 7).

The following conditions must be fulfilled before a person can become an "acceptor for honour": (i) the bill must have been "noted" or "protested" for "non-acceptance" or "better security"; (ii) the bill must not be overdue; (iii) the person accepting for honour must not be already liable on the bill; (iv) consent of the holder to such acceptance is essential. The reason is that by this means, the bill is "kept alive". (v) Acceptance can be for the "honour" of any party already liable on the bill (sec. 108); (vi) acceptance may be for whole or a part of the amount of the bill; notice to prior parties in the latter case is not necessary; (vii) such acceptance must be made on the bill itself, must be signed by the acceptor and must state for whose honour it is made (sec. 109). If the acceptance does not state for whose honour it is made, it will be deemed to be for honour of the drawee (sec. 110).

The effect of such acceptance "*supra protest*" is that the bill is treated as alive and is not considered to be dishonoured till it is dishonoured by such acceptor on presentment for payment.

The position of such "acceptor for honour" is as follows: (i) he is liable to the holder and to all parties subsequent to the party for whose

honour he has accepted, if the drawee fails to pay it; (iii) he is entitled to be indemnified by the party for whose honour he has accepted, and all prior parties to such party (sec. 111). Such an acceptor, however, will not be liable unless, (i) the bill on maturity is presented by the holder to the drawee for payment and has been dishonoured by him and is noted or protested for such dishonour (sec. 112) and (ii) unless the bill is presented to such acceptor or forwarded for presentment (if such acceptor resides elsewhere), the day next after the day of its maturity (sec. 111). In other words, such bills require to be noted and protested, once for non-acceptance and again for non-payment by the drawee.

Payment for honour

Where a bill is protested for non-payment, any person may intervene and pay it "*supra protest*", for the honour of any party liable thereon; such payment is called "payment for honour" (sec. 113).

The peculiar features of such payment are (i) the payment must be preceded by "protest"; (ii) it may be made by any party including a party already liable on the bill; (iii) no consent of the holder is necessary; (iv) such payment may be made after the bill is overdue; (v) the person paying must, before payment, declare before a "notary public", the party for whose honour he pays and (vi) such declaration must be recorded by the notary public (sec. 113).

The effect of "payment for honour" is that (i) all parties subsequent to the party for whose honour the payment is made, are discharged from liability; (ii) the payer for honour is subrogated to and succeeds to both the rights and duties of the holder, as regards the party for whose honour he pays and all parties liable to that party; (iii) the payer can recover all sums paid, with interest and proper expenses, from the party for whose honour he paid (sec. 114).

Payee: Payee means the person named in the instrument to whom or to whose order the money is directed by the instrument to be paid (sec. 7). Notice that a "payee" does not include an endorsee.

Holder: Holder is defined by sec. 8 as any person (i) entitled in his own name to the possession of a negotiable instrument and (ii) to recover the amount thereof from the parties liable thereto.

Both the above conditions are essential and must be fulfilled before any person can claim to be a "holder". As the definition shows, mere "possession" is not enough, the possession must be under a title. Thus the finder of a promissory note, bill of exchange or cheque, is not in law the "holder" thereof, as he has no right or title to it. Similarly, an endorsee under a forged endorsement and a transferee of an order bill without a proper endorsement in his favour are not "holders" in law. On the other hand, a trustee in whose name a negotiable instrument is made out, is a "holder", though the beneficial ownership of the bill belongs to another. Similarly, a person to whom a bill is endorsed by its owner for collection is a "holder".

The position of a "holder" of a bill is important for a variety of reasons : (i) he is the only person who, in law, is entitled to sue on the bill. Thus it has been held that a promissory note signed in favour of a "karta"

of a joint family, can be enforced by him only, though it may be in respect of a joint family claim. (ii) With certain exceptions, he is the only person who, in law, is entitled to negotiate it and (iii) subject to certain qualifications, he is the only person who is, in law, entitled to give a valid discharge for a bill and (iv) he is the chief person to whom all other parties are liable on a bill.

Where a promissory note is passed in favour of a joint Hindu family firm, all members who constituted the firm are "holders" of the promissory note and a suit on the promissory note by all members as plaintiffs after partition is maintainable (k).

Holder in due course

"Holder in due course" is defined by sec. 9 as "any person who (i) for consideration (ii) becomes the possessor of a promissory note, bill of exchange or cheque, payable to bearer (iii) or the payee or the endorsee thereof (iv) before the amount mentioned in the document becomes payable and (v) without having sufficient cause to believe that any defect existed in the title of the person from whom he derives his title. As the sec. says a holder in due course may be either (a) the possessor of a promissory note, bill of exchange or cheque payable to bearer or (b) the payee or endorsee thereof in other cases. As regards the last, notice that our law differs from English Law, according to which, as now held by the House of Lords (l), a "payee" is not regarded as a holder in due course.

In each case, however, three conditions must be satisfied: (i) He must be a holder for valuable consideration, (ii) before the amount has become payable, i.e. before maturity and (iii) without having sufficient cause to believe that a defect existed in the title of his transferor. To these may be added a further condition, viz. (iv) that the bill must be complete on the face of it.

As regards (i) it should be observed that a donee by way of gift of a bill of exchange or a promissory note, is not a "holder in due course", nor a holder for consideration which the law regards as void or illegal. It is not necessary that the consideration should be adequate; it is sufficient if it involves some profit or detriment which the law regards as valuable. The discountee of a bill may become a "holder in due course" if the conditions of the sec. are satisfied.

As regards (ii), notice that a holder of a bill, for value, *bona fide* and without notice of any defect, but after it has reached maturity, is not a "holder in due course", according to Indian Law. A holder of a bill which has been dishonoured by non-acceptance, but without notice of that dishonour, may become a holder in due course, if the other conditions laid down by the sec. are satisfied.

As regards (iii); our law is stricter than English Law on the subject. English Law only requires "good faith" on the part of the holder at the time of taking the instrument, i.e. honest belief in the genuineness of the title of the transferor, however negligently the belief may have been entertained. Indian Law requires not only "honest belief", but also present.

(k) Daniel v. Manmohandas, 42 Bom. L.R. 248.

(l) Jones Ltd. v. Warring & Gillow [1936] A.C. 670.

of sufficient cause for such belief. In other words, if there are sufficient indications to show the existence of a defect in the title of the transferor, the fact that the transferee took the instrument without any suspicion or knowledge of such defect, will not make him a "holder in due course".

Thus taking an instrument which is torn to pieces and then pasted together (m), or an instrument which contains erasures or which is incomplete on the face of it, does not make the taker a "holder in due course". Taking a post-dated cheque, however, is not such an act as would prevent the taker from being a "holder in due course" (n). On the other hand, the endorsee of a promissory note from the payee with notice of a prohibitory order restraining payee from receiving payment under the note is not a holder in due course (o). Notice that a holder of a bill payable to order, on which the endorsement is forged is not regarded in law as a holder in due course though all the above conditions are satisfied (p). This is because of the fundamental rule of the law of negotiable instruments, viz. that a forged endorsement is no endorsement. Such a holder, therefore, in the eye of law, takes a bill which is materially defective on the face of it, in that, being an order bill, it has on it no endorsement of the holder at all.

As regards (iv), what it means is that the title of the holder must be complete on the face of the bill. Thus an order bill, in the hands of a holder for value without notice of defect, but on which a proper endorsement in his favour is wanting, is not a "holder in due course" according to law.

In a recent Bombay case, a partner drew a post-dated cheque in the name of the partnership in his own favour and endorsed it himself in favour of a personal creditor of his own. *Held*, the latter could not be regarded as a "holder in due course" because, he should have been put on an enquiry, on seeing the endorsement, to find out whether the particular partner had authority of the partnership to draw and endorse a cheque in the form in question (p1). In a recent English case, a partner who had authority to endorse partnership cheques, endorsed such cheque but paid it in a non-partnership account. The Bank collected the money in spite of doubt, after a superficial inquiry. *Held*, the Bank was not a holder in due course of the cheque (p2).

Privileges of holder in due course

The "holder in due course" occupies a most important position in the law of negotiable instruments. He occupies this position because of certain exclusive privileges which this law accords to such holder. These are as follows :

(1) Such holder holds the bill free from any defect of title of prior parties as well as also free from personal defences available to the prior parties amongst themselves and, therefore, he can enforce the instrument according to its tenor against all such prior parties. Thus the fact that his transferor had obtained the instrument by fraud, force or for invalid consideration or under a contract which was voidable, will not make his title to the instrument defective. Similarly, the fact that there is a set-off or counter-claim available against his transferor will not debar him from recovering the full amount of the instrument.

(m) *Baxendale v. Bennet* (1878), 3 Q.B.D.

(n) *Hithcock v. Edwards* (1889), 60 I.T.

(o) *Subramania v. Chokalingam*, 46 Mad.

(p) *Hansraj v. Rattanji*, 24 Bom. 65.

(p1) *Sunderdas v. Liberty Pictures, A.I.R.*

(1956) Bom. 618.

(p2) *Baker v. Barclay's Bank* (1955), 2 All E.R. 571.

(2) Conditional delivery or delivery for a special purpose cannot be pleaded against such holder.

(3) Such a holder can transfer all his rights and privileges to a holder (for value or without value), provided the latter has not been a party to the fraud himself (sec. 53).

(4) An inchoate instrument converted into a bill, though not according to the authority granted, if properly stamped, is valid, if it subsequently comes into the hands of such a holder.

(5) Estoppels against acceptor: the acceptor is precluded from denying against such holder, (i) the existence of the drawer, the genuineness of his signature and his capacity to draw the bill; (ii) in case of order bills, the capacity of the drawer to endorse (though not the genuineness of the endorsement) and (iii) in case of bills payable to the order of a third person, the existence of the payee, and his capacity to endorse (though not the genuineness of his signature) (see sec. 120).

(6) Estoppels against drawer: a drawer is precluded from denying against such holder (i) the existence of the payee; (ii) his capacity to endorse (though not apparently the genuineness of his endorsement) (see sec. 120).

(7) Estoppels against indorser: an indorser of a bill is precluded from denying against such holder (i) the genuineness and the regularity of the drawer's signature and (ii) of all previous endorsements (see sec. 122).

(8) The acceptor of a bill is precluded from contending against such holder that the drawer of the bill is fictitious, if it is payable to order and is endorsed by the same hand, as the drawer's and purporting to be the drawer's (sec. 42). It is because of the above privileges which are accorded to a "holder in due course", that such holder occupies an almost unique position in the law of negotiable instruments.

Payment in due course

This is defined by sec. 10 as payment (1) in accordance with the apparent tenor of the instrument (2) in good faith and (3) without negligence (4) to any person in possession of the instrument (5) under circumstances that do not afford a reasonable ground for believing that the person was not entitled to receive the amount mentioned in the instrument.

The question of "payment in due course" becomes important from the point of view of the drawee or acceptor of a bill. In order to obtain a complete and valid discharge against the drawer, the payment of a bill by its acceptor must amount to a "payment in due course". The payment of a bill by an acceptor, otherwise than by a payment in due course, leaves him liable to the drawer; he is not entitled to debit such payment to the drawer's account. In order to amount to a "payment in due course", the following five conditions must be satisfied:

(i) The payment must be in accordance with the directions contained in the bill. The payment of a larger or lesser amount or of something other than what the order directed, will not make it a payment in due course. Notice that payment of a bill before maturity is not a payment in accordance with the tenor of the bill. In order to be such, it must be paid at or at maturity.

(ii) It must be honestly made, i.e. in the *bona fide* belief that the person demanding payment is legally entitled to it.

(iii) The drawee must not be guilty of any negligence in making the payment, e.g. paying a person who presents a specially endorsed bill without inquiry as to his identity, or paying an order bill without noticing the absence of a proper endorsement.

(iv) The person demanding payment must be in possession of the instrument. The law requires that the acceptor before payment must insist on seeing the instrument and on payment, to require the holder to deliver it up to him.

(v) The last requirement is analogous to a similar requirement in case of a holder in due course. Thus payment of a bill by the acceptor after the drawer has countermanded payment (q), or of a bill in the hands of a person whose possession appears to be suspicious is not such payment.

(vi) The payment must be made by a party liable on the bill, and not by a stranger. This is because no stranger can, in law, be an acceptor of a bill. The important point to notice is that where all the above conditions are duly satisfied, the drawee or acceptor obtains a complete discharge as against the drawer in respect of the bill, even if the payment is actually made by him to a person who has no legal title to receive it, the only exception to the rule being in cases of forgery.

Indorser, indorsee and indorsement

Secs. 15 and 16 define who are respectively an indorser, and an indorsee. The party who indorses a bill is called an "*indorser*", the person in whose favour the bill is indorsed is called the *indorsee*.

"*Indorsement*" is defined by the same sec. as follows: "Where the maker or holder of a negotiable instrument (1) signs his name (2) otherwise than such maker (3) for the purpose of negotiation (4) on the back or face thereof or on a slip of paper annexed thereto or a stamped paper intended to be completed as a negotiable instrument, he is said to "*indorse*" the bill.

Law does not require any particular form of words to be used in order to make an indorsement valid. It must, however, conform with the name mentioned in the bill. A bill in favour of R. K. Dalal or order is not properly indorsed if the indorsement is signed as "Dalal" or "R. Dalal". If the name of the indorsee is incorrectly given, such indorsee can indorse the bill by signing in the same way and thereafter signing it with his correct name. The indorsement should be made with a view to negotiate the bill. Handing over a bill to another for a special purpose (called "*escrow*") with a proper indorsement thereon, does not amount to "negotiation". Indorsement does not amount to a complete negotiation, the law requires indorsement and delivery for this purpose. Indorsement may be made on the back or face of the bill, or on an attached slip of paper (called "*allonge*"). An incomplete instrument also can be validly indorsed, as the sec. says.

Varieties of bills of exchange

Bills of exchange are of various types. A bill may be (a) an inland or (b) a foreign bill.

An *inland bill* is a bill (i) which is drawn in India and (ii) which is either payable in India or drawn on a person residing in India (sec. 11). All bills which are not inland bills are *foreign bills* (sec. 12). Thus a bill drawn in Bombay, payable in Calcutta on a person in France is an inland bill; similarly, a bill drawn in Bombay on a person in Calcutta but payable in France is also an "inland bill".

On the other hand, a bill drawn in France on a person in Bombay and payable at Calcutta is a "*foreign bill*". The distinction is important because under sec. 104, foreign bills must be protested for dishonour when such protest is required by the law of the place where they are drawn. Protest is optional in case of "inland bills".

A bill may be (a) a bearer or (b) an order bill. A bill is said to be *payable to bearer* when (i) it is expressed to be so payable or (ii) on which the last or only indorsement is an indorsement in blank (sec. 13, Expl. ii). A bill is an *order bill* when (i) it is expressed to be so payable or (ii) which is expressed to be payable to a certain person, without containing words prohibiting transfer or indicating an intention that it shall not be transferable (sec. 13, Expl. i) or (iii) which is payable to the order of a certain person (Expl. iii). Thus a bill payable to "A or order", or to "A" or "to the order of A", is an "order bill". But a bill payable to "A only" is not an "order bill". The second type is now regarded as an order bill by virtue of the special provisions of sec. 13, which overrule the decision of the Bombay High Court to the contrary (r).

Notice that a bill is not invalid because it is non-negotiable. A bill "payable to bearer on demand", however, is illegal, and void. This is because under sec. 31 of the Reserve Bank Act, the power and right to issue such bills has been exclusively reserved to the Reserve Bank of India. The only exceptions to this rule are (1) cheques and (2) banker's drafts.

"Bill in a set"

This is a type of bill in which instead of there being a single bill, the bill is drawn in several parts, all constituting together a single bill. Thus a bill may be drawn in a set of three or four or as many parts as the exigency of the case may require. Bills are drawn in this form where they have to be sent over long distances and there is a consequent danger of loss or delay.

The following are the requirements of such a bill: (i) each part must be numbered; (ii) each must contain a reference to the others; this is essential, because if this is omitted, each part will constitute a separate bill; (iii) each must contain a provision that it shall be payable only as long as other parts are unpaid (sec. 132).

Such bills have the following peculiarities: (i) the whole set constitutes one bill; (ii) all parts must be handed over to the same holder; (iii) if one part is paid, the whole bill is extinguished; (iv) all parts require to be stamped (see Stamp Act); (v) only one part requires to be accepted; (vi)

the drawee is entitled to accept and pay in due course, the part first presented.

Notice that (i) if different parts are handed to or endorsed to different persons, the party in question is liable on each part as a separate bill; (ii) similarly, if more than one part is accepted, the acceptor is liable on each part as a separate bill; (iii) as between holders in due course of different parts, he who first acquired title to his part is entitled (a) to the other parts and (b) to payment under all the parts (sec. 133).

Accommodation bill

This may be defined as a bill which does not represent exchange of values, but which is drawn by one person, and accepted by another, without consideration, merely to enable the drawer to raise money on the bill by discounting it. The party accommodating is called the "*accommodation party*", the party accommodated, is called the "*accommodated party*". "Accommodation" may be effected by a person either drawing a bill or accepting a bill or endorsing a bill without consideration. Where a person is induced to endorse a bill without consideration, he is called a "*backer*", and the operation is called "*backing the bill*".

The rules with regard to such bills are: (i) the "*accommodation party*" is liable as any ordinary party to a holder for value of the instrument (even though the holder was aware of the fact that the party was only an "*accommodation party*") (sec. 43); (ii) if the "*accommodation party*" has to pay, he can recover the amount paid from the "*accommodated party*" by a suit (sec. 43).

The obligations of an "*accommodated party*" are: (i) he undertakes to take up the bill on the due date. (ii) In the alternative, he must provide the "*accommodation party*" with funds to meet the bill on the due date. (iii) Lastly, if the "*accommodation party*" has to pay the bill, he must indemnify such party for payment duly made by him in respect of the bill.

Notice that under sec. 59, "*accommodation bills*" can be negotiated after maturity and the holder of such a bill (i) in good faith and (ii) for valuable consideration (iii) even though after maturity, is entitled to enforce payment thereof from all prior parties thereto. This is an exception to the general rule, viz. that the transferee of a bill after maturity, acquires the same title to it as the transferor had even though he may have taken it in good faith and for value (sec. 59). Notice further that (i) under sec. 76, non-presentment of an accommodation bill to the drawee for payment does not discharge the drawer. Similarly, (ii) failure to give notice of dishonour, does not discharge all prior parties to the bill, when the bill is an accommodation bill (sec. 98).

Inchoate bill

This means an incomplete bill, i.e. a bill in which a material particular necessary to make it a complete bill is missing, e.g. where the signature of the drawer or the drawee's name or the payee's name or the amount is missing. Where such an "*inchoate bill*" is handed over by a person to another by way of negotiation, the law impliedly confers on the transferee an authority to fill up the blanks. Thus where the payee's name is omitted, the person taking such instrument from the maker can put in his own name as payee.

Two conditions must be fulfilled before an "inchoate bill" can be thus completed by the holder: (i) The omissions must be filled up within a reasonable time. The lapse of a year before filling up an "inchoate cheque" has been held to be unreasonable (s). (ii) As against a person who became a party to such instrument before it was so completed, the authority delegated must have been strictly observed, in order to make such person liable on the bill. Of course, when a holder in due course is concerned, the fact that such authority was exceeded or dishonestly exercised, will not be a good defence on the part of parties liable in respect of such bills.

A particular case of such a bill is contemplated by sec. 20. Where a person (i) delivers to another (ii) a properly stamped paper (iii) with an incompleted bill thereon, e.g. the amount being omitted to be mentioned, (iv) the holder of such a bill can complete the bill for any amount, not exceeding the amount covered by the stamp; (v) if a bill so completed gets into the hands of a holder in due course, he can recover the full amount thereof from the maker, though (vi) as between the maker and the person completing the instrument only the amount authorised by the former to be put can be recovered by the latter.

Notice that, as has been recently held, the principle of estoppel under sec. 20, only applies to nego. instruments. Thus it does not apply to cheques marked "not negotiable" (t). It has been doubted whether the transferee of an inchoate instrument can be called a "holder in due course", because the instrument is obviously incomplete, on the face of it (u).

Undated bill: Where the date of a bill is omitted and where the date of the acceptance of a bill, payable a fixed period after sight, is omitted, any holder may insert the true date of issue or acceptance as the case may be. If the holder, however, *bona fide* inserts a wrong date and in all cases where a wrong date is inserted, such date shall be regarded as the true date, against a holder in due course. Under sec. 18(b), every negotiable instrument bearing date, is presumed to be made or drawn on such date.

Ambiguous bill: This means an instrument which can be construed either as a promissory note or as a bill of exchange, e.g. a bill drawn by a person on himself in favour of a third person; similarly, where the drawee is a fictitious person or a person unable to contract (sec. 17). The law with regard to such bills is that the holder may, at his choice, treat such instrument as a bill or a note. As he elects, so the nature of the instrument will thereafter be regarded as determined. Where the amount of a bill in words and figures differs, the words shall prevail (sec. 18).

Fictitious bill: This means a bill of which the drawer, the drawee or the payee is a fictitious person. The word "fictitious" has two meanings: it means (i) a non-existing person and (ii) a pretended person, i.e. a person other than the actual person intended by the parties, e.g. when the name of a payee is inserted in a bill by way of pretence merely, without any intention that payment shall be made in conformity therewith (v).

In English Law, a bill in which the payee is a fictitious person is always regarded as payable to bearer. The result is that if such a bill is an order

(s) Griffiths v. Dalton (1940), 2 K.B. 264.

(t) Wilson & Meeson v. Pickering (1946),
1 A.E.R. 394.

(u) Tarachand v. Sikri Bros., 55 Bom.
L.R. 231.

(v) Bank of England v. Vagliano (1891),
A.C. 107.

bill, with the endorsement forged by an unauthorised person, the drawee will be protected in paying him, because in such a case the forged endorsement does not matter (v). A bill in which either the drawer or the payee is fictitious cannot be enforced by law, even if accepted by the drawee. The only exception is in favour a "holder in due course", as against whom the acceptor is not entitled in law to plead the fact that the drawer is fictitious, if the bill being payable to the drawer's order, he claims under an endorsement purporting to be the drawer's and made in the same hand as the drawer's signature (sec. 42).

Bills payable on Demand, at Sight or on Presentment

Bills may also be classified according to the time at which they are payable: (i) A bill or note *payable on demand* becomes payable on the date on which it is drawn. No demand is necessary in this case and limitation runs from the date of the bill or note.

(ii) A bill or note payable "*at sight*" or "*on presentment*", becomes payable after the instrument is "*sighted*" or "*presented*" to the drawee with demand for payment (sec. 21). A demand in such a case is necessary and limitation will begin to run only from the date the demand is made.

(iii) A bill payable "*after sight*" means after acceptance or "*noting*" or "*protesting*" for non-acceptance and in case of a promissory note, after presentment for sight (sec. 26). A bill or note payable "*after sight*" must mention the particular period "*after sight*" at which the instrument is to be payable. The period in case of such a bill is counted from the date of acceptance or "*noting*" or "*protesting*" for non-acceptance and in case of such a promissory note, from the date of presentment of the same.

(iv) A bill payable "*after date*" means after date of the bill. Notice that under sec. 19, where a bill or note does not specify the time at which it is to be payable, it is regarded in law as payable on demand.

Rules as regards Maturity

Certain rules have been laid down by the Act for determining the question when a bill in law becomes payable, i.e. when it reaches "*maturity*". "*Maturity*" means the date on which a promissory note or a bill of exchange falls due (sec. 22). Thus (i) a bill or pro. note payable on demand is payable on the date it bears (sec. 21). (ii) A bill or pro. note payable "*at sight*" or "*on presentment*" is payable when "*sighted*" or "*presented for payment*" (sec. 21). (iii) A bill or pro. note payable "*after date*" or "*after presentment*" or on a specified day, matures on the third day after the day on which it is expressed to be payable (sec. 22). The extra days (three in number) which are allowed in case of such bills and pro. notes, are called "*days of grace*". They are not available in case of bills and pro. notes payable "*on demand*", "*at sight*" or "*on presentment*".

Calculating Maturity

Certain rules have been laid down by the Act for calculating the maturity of a bill. These are: (i) if the date on which a bill or pro. note falls due, is a public holiday, the instrument is deemed to fall due on the next preceding business day (sec. 25). Public holidays under the Nego.

Inst. Act are Sundays, New Year's Day, Christmas Day, (if last two fall on Sunday, the following Monday), Good Friday, and any other day declared by the Central Government to be a public holiday under the Act (*ibid*).

(ii) In case of bills or pro. notes "after date", "after sight" or "after a specified event", the day of the date of presentment for acceptance or sight, of protest for non-acceptance and of the happening of the event is to be excluded (sec. 24).

(iii) In case of bills and pro. notes payable a certain number of months, "after date" or "after sight" or "after certain event", the period shall be deemed to terminate on the day of the month corresponding with the day on which the instrument is dated or is presented (for acceptance or sight) or is noted or protested for non-acceptance or on which the event happens (sec. 23). If there is no corresponding day in such a month, the last day of the month is to be taken as the day of maturity (sec. 23). Thus a bill drawn on 28th Jan., payable a month after date, matures on the third day after 28th Feb. Similarly, a bill drawn on 30th or 31st Jan. will also mature on the third day after 28th Feb. (or 29th Feb. in a leap year) under the second part of sec. 23.

Usance

"*Usance*" is the technical name for the time fixed by custom within which bills drawn in one country and made payable in another country are to be paid. The period varies with different countries. In most continental countries the period is generally three months; for bills on Lisbon and Oporto 90 days; for bills on Calcutta and Bombay, 30 days. Drawers generally consult their own convenience or that of the firms with whom they deal in fixing the period after which the bill will be payable.

Overdue Bill

This is a bill which is negotiated after maturity. A person taking such a bill takes it subject to any defect in the title of his transferor, whether he was aware of the same or not and whether he paid value for it or not. A bill payable on demand is overdue when it has been in circulation for an unreasonably long time. As regards other kinds of bills, their maturity depends on their date and wording. A bill known by the holder as dishonoured, is treated as an overdue bill, so far as he is concerned.

Lost Bill

The owner of a lost bill or note does not lose his title to recover the amount of the instrument from the parties liable thereto. He can receive the amount on giving a proper indemnity (*w*). Secondly evidence of the bill or note has to be given or suit may be brought on the original consideration for which the bill or note was passed. Under sec. 118 a lost bill or note is presumed to be duly stamped. Further, under sec. 45-A, the holder of a lost bill, which is not overdue, is entitled to claim a duplicate from the drawer, after giving an indemnity to him against all persons in case the bill is subsequently found. If the drawer, in the above circumstances, refuses to give a duplicate, he can be compelled to do so by means of a suit.

(w) *Hansard v. Robinson* (1827), 7 B. & C. 90.

The bill however must not be overdue. If loss occurs after maturity, apparently there is no right under the sec. to claim a duplicate from the drawer. Similarly, the sec. makes no provision for lost pro. notes. Decided cases in India, however, following the English rule have recognised the right, both in case of non-matured and matured bills as well as pro. notes of the same nature (x). The owner of a lost bill or note is well advised to give a notice of such loss to the acceptor or drawee without undue delay, as well as a public notice by advertisement.

The loss of a bill or note does not absolve the holder from the obligation of making an application for payment on the due date and from giving notice of dishonour if the bill is dishonoured. Protest can also be made on a copy or written particulars of the lost bill. Notice that the holder of a duplicate bill cannot claim payment, if the original has been duly paid by the party liable thereon.

Destroyed Bill

The Act makes no provision for destroyed bills, but it is presumed that the above principles will apply in case of destroyed bills also. An action on a destroyed bill can be brought, the plaintiff in such a case giving proof of its disruption and of its contents (y). No question of indemnity arises in such a case.

Bankers' Drafts

These are orders addressed by one bank to another Bank or by a bank to its branch, either abroad or in their own country, directing the latter to pay a specified sum of money to a named person or his order. When the drawer and the drawee of these drafts are the same, it is permissible to regard them as cheques. Under English law, however, they are not regarded as cheques, so that the special rules as regards crossing do not apply to them. In India, it is otherwise, as new sec. 131A of the Act makes all rules laid down with regard to crossed cheques in sec. 123-131, applicable to drafts defined by sec. 85A. Thus a banker collecting a draft for a customer will now be protected by sec. 131; though the Bombay High Court had held otherwise, before the new amendment (z).

These drafts are drawn either against cash deposited at the time of their purchase or against debits to current account with the banker. The purchaser of the draft generally hands in the particulars. Bankers charge a small commission for their services. As in case of cheques, the drafts can be made payable to drawer on demand, without any legal objection thereto, as the Reserve Bank Act, sec. 31, specially allows such drafts to be issued.

Under sec. 85A, where a draft, being an order to pay money drawn by one office of a bank on another office and payable to a person or order on demand, purports to be endorsed by or on behalf of the payee, the banker is discharged by payment in due course. The protection afforded to a banker in respect of cheques bearing forged endorsements is thus secured for demand drafts of the above nature.

(x) *Udho Ram v. Hemraj* (1924) Lah. 198.

(y) *Wright v. Maidstone* (1855), 24 L.J.

Ch. 623.

(z) *Sanyasalingam v. Exchange Bank of India*, 49 Bom. L.R. 309.

"A banker's draft is a bill drawn either on demand or otherwise by one bank on another in favour of a third party or by one branch of a bank on another branch of the same bank or by the head office on a branch or vice versa". It is a negotiable instrument and *prima facie*, therefore, the relationship between the holder of the draft and any prior party (e.g. the bank) is that of a creditor and debtor.

But where money is paid to a banker for the express purpose of being transmitted to and paid to another person at a different place, the bank holds the money as agent for the customer. These moneys do not become a debt, because as evidence of the payment, a draft is given by the receiving bank to the customer. If such moneys are transmitted by the banker to its branch at the other place for the purpose of being paid over to the payee, the branch also holds the moneys as agent for the payee and the closing of the branch before actual payment cannot affect the payee's rights (a).

Documentary Bills

These are bills or drafts to which shipping documents are attached. These are bill of lading, insurance policy and a copy invoice (generally in triplicate). The draft or bill is generally endorsed to the order of the collecting bank. The bill of lading however is generally endorsed in blank. A slip is also often annexed, which advises the bank to hand over the documents either against acceptance or payment (D/A or D/P).

Treasury Bills (India)

The Government of India is under obligation to make periodical remittances to the British Treasury in sterling. These remittances are made, by the British Government drawing bills on the Government of India, which are taken up by British merchants at tender value and are disposed of in India in discharge of their trading liabilities. The procedure adopted is as follows: The India Government periodically advises British Government of the amount available for remittance. The British Government thereupon issues bills (called Treasury Bills) in Rupees on the Indian Treasuries at Calcutta, Bombay, or Madras. Tenders are submitted to the British Treasury by Banking and Discount Houses in England for such bills, they having to make payments in India in rupees. They are allotted to the highest bidders. Thus the indebtedness of India to Britain and vice versa is wiped off.

Letters of Credit (L/C)

They are orders by bankers on other bankers or on their own branches to grant a specific credit to the holder of the letters. They take two forms: (i) by one Bank on another requesting the latter to allow the bearer to draw upto a particular amount; (ii) by a banker to bearer allowing him to draw on itself for a particular amount for a specified period, generally six months. When such a credit is allowed without any conditions, it is called a "*clear letter of credit*". Where conditions are attached to it, e.g. that an invoice or bill of lading should accompany the same, it is called a "*documentary letter of credit*". "*Marginal letter of credit*" means a letter, the

margin whereof states the terms of issue. Where the authority granted by the bank to the holder, is revocable by the bank, it is called a "*revocable or unconfirmed letter of credit*"; where it is not liable to be revoked, it is called a "*confirmed or irrevocable letter of credit*".

These letters are useful for international commercial transactions and also for facilitating foreign travel. "Circular letters of credit" are requests by a bank to its agents or correspondents in foreign countries to honour the cheques or drafts of the holder, which the issuing bank undertakes to honour on presentation. These are far more commonly used for foreign trade, e.g. Cook's Circular Letters. "Travellers' cheques" are also of the same nature. A letter of credit is not a negotiable instrument (b).

Where the buyer's credit is not firm in the seller's country, it is often made a condition of the contract of sale of goods and particularly, if it is a contract on C.I.F. terms, that the buyer shall open a confirmed credit in a bank in the seller's country. In such a case, it becomes the duty of the buyer to procure the bank to issue an irrevocable credit in favour of the seller. By doing so, the bank undertakes to the seller to accept drafts drawn upon the bank for the price of goods, against tender of the bill of lading, invoice and policy of insurance. The contract thus created between the seller and the bank is separate from, though ancillary to, the original contract between the buyer and the seller and the bank therefore is not entitled to rely on the terms of the contract between the buyer and the seller for the purpose of refusing to the seller payment against documents, e.g. on the ground that goods are not according to contract (c).

An irrevocable letter of credit cannot be withdrawn without the assent of the beneficiary. If the banker revokes the same, he will be liable in damages (d). Notice that insolvency of the banker issuing an irrevocable letter of credit does not justify the shipper for whose benefit the letter of credit is issued to repudiate his contract (e).

It has been recently held in England that where a contract requires the buyer to provide confirmed credit facilities to the seller, the credit must be opened and confirmed by the buyer and be made available by him to the seller before the seller's time of performance begins (f).

LIABILITY OF PARTIES

Capacity of parties: The general rule is that every person (including a minor), capable of entering into a contract according to the law to which he is subject, can draw, endorse, deliver, accept or negotiate a bill of exchange. A minor however who draws, endorses, delivers, accepts or negotiates a bill of exchange, thereby makes liable on the bill, all other parties thereto, except himself (sec. 20). As regards incorporated companies, they can do any of these things only if empowered to do so by their constitutions (ibid).

Liability of an agent: A party, in order to be liable on a bill of exchange is not required by law necessarily to sign his name personally on the bill. Liability may also be incurred, vicariously, e.g. by an authorised agent signing such instrument on behalf of such party (sec. 27).

(b) Orr & Barber v. Union Bank of Scotland, 24 L.T. (O.S.) 1.

(c) Urquhart Lindsay & Co. v. Eastern Bank (1922), 1 K.B. 318.

(d) Ibid.

(e) Re Agra Bank (1867), 5 Eq. 160.

(f) Pavia & Co. v. Thurmann Neilson (1957), 1 All E.R. 492.

Two conditions must be fulfilled, however, before this result can follow : (i) the agent must be duly authorised by his principal to draw, endorse, negotiate, deliver or accept a bill of exchange as the case may be ; (ii) he must have exercised the authority as an agent.

As regards the first, sec. 27 provides that a general authority to transact business and to receive and discharge debts, does not confer upon the agent an authority to accept or endorse bills of exchange. Similarly, an authority to draw a bill of exchange does not by itself confer an authority to endorse a bill, neither does an authority to endorse, confer an authority to accept a bill. Authority in each case must be strictly proved in order to make the principal liable on the bill. In this connection, notice that a partner in a trading firm has implied authority on behalf of the partnership, to draw, endorse, accept, deliver and negotiate bills of exchange in the name of and on behalf of the partnership. A partner in a non-trading partnership has no such implied authority. In case of such a partnership, therefore, express authority to a partner will be required to be proved.

As regards the second condition, notice that sec. 28 specifically lays down that an agent signing a promissory note, bill of exchange or cheque (i) without indicating thereon that he signs as agent or (ii) without excluding his personal responsibility, becomes in law personally liable on the instrument, except to persons who induced him to sign on the representation that the principal alone would be held liable. In other words, it must clearly appear on the face of the instrument that the person signing it is merely an agent for another and that, therefore, he does not agree to be personally liable thereon.

Thus a bill signed as R. K. Mehta by his agent P. K. Dalal or R. K. Mehta per pro. "P. K. Dalal" or "P. K. Dalal as agent for R. K. Mehta" will not make P. K. Dalal (agent) personally liable. "Per Pro." (per procuratum) here means "on behalf of". If however the agent signs in his own name without distinctive words showing agency, he will be personally liable. Thus a bill signed by "P. K. Dalal, agent for R. K. Mehta", or "By A. B., director of C. R. Co." (g) will make P. K. Dalal and A. B. (agents) personally liable on the instrument. The question in each case depends on the true construction of the words used.

Legal Representative : The same principles apply in case of legal representatives who sign nego. insts. as executors or administrators of a deceased person. In such cases the legal representatives are personally liable unless, as sec. 29 says, they expressly limit their liability to the extent of the assets received. Thus legal representatives, in order to exclude personal liability, must expressly limit their liability to the amount of the estate of the deceased in their hands.

In England the law is different ; an executor signing a bill and describing himself as executor has been held not to make the executor personally liable. As pointed out by the Privy Council (h), it is always a question of fact, to be decided on the construction of the words used in each case ; the English doctrine of admission of assets having no application to India.

Liability of the drawer

As distinguished from the liability of the maker of a promissory note (which is primary), the liability of the drawer of a bill of exchange is only

(g) *Shree Lal v. Lister Antiseptic Co.*, 52 Cal. 802.

(h) *Sir Jamsedji v. Sorabji*, I.L.R. (1940), Bom. 534.

boundary. As sec. 30 points out, the drawer of a bill is liable to compensate the holder in case (i) the bill is dishonoured by the drawee or acceptor (either before or at maturity) and (ii) if due notice of dishonour is given to him as required by the Act. The liability arises on contract, and is conditional. Till both the above conditions are satisfied, the holder cannot, in law, have any claim against the drawer on the bill. Notice that under sec. 118, the drawer is estopped from denying the existence of the payee and his then capacity to endorse, as against a holder in due course.

Liability of the drawee

The drawee of a bill is under no obligation, contractual or otherwise, to the holder of a bill to accept it. He therefore incurs no liability to the holder by refusing to accept the bill. His liability only arises if and when he accepts the bill and thus becomes, an acceptor of the bill.

Liability of the acceptor

His liability arises under the contract represented by his acceptance of the bill. It is primary, and not secondary, as in the case of the drawer. The liability is also absolute and unconditional (unless expressly made otherwise). Thus the death or insolvency of the drawee does not affect it. Similarly, if acceptance is against documents, non-arrival of the goods will not absolve him from liability on the bill (i). As sec. 32 lays down, in absence of a contract to the contrary (i) the acceptor of a bill before maturity is bound to pay the amount thereof at maturity, according to the apparent tenor of the acceptance. (ii) If the bill is accepted after maturity he is bound to pay the amount to the holder on demand; (ii) if he fails to pay the amount as above, he becomes liable to compensate any party to the note (including the holder) for the loss caused to him by such default.

Notice that the liability of the acceptor is subject to a contract to the contrary. Thus an "accommodation acceptor" is not liable to compensate for failure to carry out his undertaking (except of course to a holder in due course). Further, his liability is conditional by the tenor of his acceptance. Thus if the acceptance is qualified, he cannot be made absolutely liable on the bill, e.g. if acceptance is for part of the amount or subject to some additional terms. Thirdly, his liability does not arise by mere acceptance but only on acceptance and delivery.

Notice that he is liable to all parties interested in the bill and not to the 'holder' alone. Under sec. 121, an acceptor is estopped from denying to a holder in due course the capacity of the payee to endorse the bill, if the bill is an order bill. The estoppel however does not include the genuineness of the payee's signature. Further, an acceptor of a bill on which an endorsement is forged is not relieved from liability on the bill, if he knows or had reason to believe that the endorsement was forged when he accepted the bill (sec. 41). Similarly, as against a holder in due course, the acceptor cannot escape liability, on the ground that the drawer and payee of a bill payable to the drawer's order, are fictitious if such holder is claiming under an endorsement in the same hand as the drawer's signature and purporting to be made by the drawer (sec. 42).

(i) *Motishaw & Co. v. Mercantile Bank of India*, 41 Bom. 567.

Liability of indorser

Every indorser of a bill, in absence of a contract to the contrary, is liable under sec. 35, to every subsequent holder of the bill, in case of the dishonour of the bill to compensate him for the loss caused thereby, provided due notice of dishonour is given to or received by him. An indorser after dishonour is liable as on an instrument payable on demand. The liability of an indorser is a conditional liability. He is liable on the instrument provided (i) the instrument is dishonoured, (ii) due notice of dishonour is given to or received by him and (iii) provided there is no contract to the contrary. When liable, he is liable (i) for the whole amount of the instrument and (ii) as on an instrument payable on demand.

An endorsement may be either absolute or conditional (see seq.). Where the endorsement is conditional, the indorser will not be liable unless the conditions are fulfilled. An indorser may by proper words exclude all liability on the instrument, e.g. by indorsement "sans recourse". Of course the indorser's liability arises only after endorsement *and* delivery of the instrument.

Notice that under sec. 40, where the holder of a negotiable instrument, without the consent of the indorser, destroys or impairs the indorser's remedy against a prior party to the bill, the endorser is discharged from liability to holder, as if the bill had been paid at maturity. Thus if a bill bears endorsements of various persons through whose hands it has passed, the cancellation of any of the intervening endorsements by the holder will absolve the last indorser from liability to the holder, because the action of the holder has deprived the last indorser of his right as surety against such prior indorser (see seq.). An indorser who pays off a holder is entitled to the benefit of all securities held by the latter in respect of the bill just as a surety who pays off a creditor would be (j).

Liability of intervening parties

Secs. 36 to 39 deal with the question of the liability of the various parties to a bill of exchange *inter se*. Three principal rules are laid down :

(i) As regards a holder in due course, each "prior party" to a bill of exchange is liable to him till the instrument is duly satisfied (sec. 36). "Prior party" here includes all the intervening endorsers as well as the drawer and the acceptor. The meaning of the sec. is that a holder in due course can hold any one or more or all the above parties liable for the amount of the instrument. This is because, qua such holder, the liability of the above parties, is both joint and several (k).

(ii) As between such prior parties, the drawer of a bill of exchange (until acceptance) and the acceptor (after acceptance), are, in absence of a contract to the contrary, liable on the bill as principal debtors, while the other parties, i.e. intervening endorsers, are liable (subject to the same limitations) only as sureties for the drawer or acceptor as the case may be (sec. 37).

(iii) As between the parties liable as sureties only as aforesaid, each prior party is (in absence of a contract to the contrary) liable thereon as a principal debtor to each subsequent party (sec. 38). The above rules are

(j) *Duncan v. North & South Wales Bank* (1881), 6 A.C. 1.

(k) *Basanta v. Kolahat*, 1 All. 392.

the fundamental rules as regards the liability of parties to a negotiable instrument. They may be worked out as follows: A draws a bill of exchange on B (which is accepted by B) in favour of C or order. C endorses it in favour of D and D to E, who takes as a holder in due course. In such a case E can sue, at his choice, either A, B, C or D or all of them or any or more of them for the amount of the bill, in case of dishonour (Rule i). As between A, B, C and D, A before acceptance and B after acceptance are liable as principal debtors, while C and D are liable only as sureties (Rule ii). As between C and D, C is liable as principal debtor, while D is liable as a surety for C (Rule iii). Thus if E files a suit against D to recover the amount of the bill, D will have a right of action against A as principal debtor. D will also have a right of action as against C, as being surety for C for the amount.

(iv) A fourth rule is added to the above by sec. 39 under which, when a holder enters into a contract with the acceptor to release him from liability (sec. 134, Contract Act) or to give him time (sec. 135 *ibid*), the "sureties" mentioned above will be discharged unless the holder has expressly reserved his right against them. Notice that an endorsee of a promissory note can only sue on the endorsement. He has no right or title to sue on the original debt as he is not entitled to the debt (l).

Liability in case of bearer instrument

The rules mentioned above only govern cases where a nego. inst. has been transferred by an indorsement and delivery. Instruments payable to bearer, however, do not require indorsements and are capable of being negotiated by delivery only. When a nego. inst. has been thus transferred by delivery only, the transferee is not in law regarded as the indorsee, nor the transferor the indorser of the instrument. The above rules therefore will not apply to such a transfer, which law regards as in the nature of a sale. The transferee of such an instrument therefore has no right of action on the instrument against his transferor to recover the amount paid by him in case of dishonour. It has been held further that in such a case he cannot recover against his transferor as on a failure of consideration.

This does not mean however that the transferor of a bearer instrument is in no event liable to the transferee for loss caused to him by the dishonour of the instrument. The law in case of such transfers, holds the transferor liable to the transferee upon certain implied warranties. These are as follows:

- (i) That the signatures on the instrument are genuine.
- (ii) That the instrument is valid in law.
- (iii) That the parties concerned were competent to contract.
- (iv) That the transferor had a right to transfer the instrument.

The first protects the transferee against forgery; the second against invalidity of the instrument on the ground of stamp or otherwise, the third against the possible minority or other incapacity of parties and the fourth against illegal possession of the instrument. The transferee of a bearer instrument, therefore, if he fails to recover the amount of the instrument from the parties liable thereon, is entitled to proceed against his transferor

for the loss so caused to him, if his case falls within any of the four classes mentioned above (see sec. 47). Notice that a bearer instrument means both an instrument expressed to be payable to bearer as also an order instrument which is indorsed in blank (sec. 13).

Discounting Bills

It has been held by the Privy Council (*m*) that drawers of a bill of exchange who discount them with a bank are bound, in case of dishonour by the acceptors, to compensate the holder for value (i.e. the bank), unless they, i.e. the drawers, can show that when they discounted the bills, they bargained with the bank that the transaction was to be without recourse. To relieve the drawers from their liability and to limit the bank's *prima facie* right of recourse against themselves (the drawers), the latter must show some contract with the bank to that effect or some breach of contract or duty on the bank's part which would have that effect in law. Where therefore the drawers, when discounting their drafts with the bank, made over documents of title (e.g. bill of lading, etc.), to the discounting bank and the drafts were marked D/A, *held*, the bank was justified in surrendering the documents to the acceptors on their acceptance of the drafts and if thereafter the drafts were dishonoured by non-payment, the drawers could not escape their liability to re-imburse the discounting bank for the loss suffered by it.

Consideration

Four rules are laid down in this connection: (1) Like every other contract, a contract represented by a nego. inst. must be supported by consideration in order to be effective. Thus sec. 43 provides that a nego. inst. made, drawn, accepted, endorsed or transferred without consideration (or for a consideration which afterwards fails), creates no obligation of payment between the immediate parties thereto, i.e. between the drawer and the drawee, or acceptor; between the drawer and payee, the indorser and the immediate endorsee. Thus no party for whose accommodation a bill has been drawn, accepted or indorsed, can sue the "accommodation party" on the bill, if he has paid the amount thereof (sec. 43). Again, where a bill drawn by A in favour of B is endorsed by B in favour of C without consideration, C cannot recover anything on the bill against B as his indorser, in case the instrument is dishonoured.

The sec. however goes on further to lay down an important exception to the above rule, viz. that if any such party transfers the instrument (with or without indorsement) to a holder for consideration, such holder and every holder deriving title through him, can recover the whole amount of the instrument from his transferor or any prior party thereto. The meaning of the above rule is that though absence of consideration may be a good defence as between parties who are in immediate relation on the bill, it affords no defence to a suit brought by a subsequent holder for value of the bill. Such a holder for value and those deriving title from him are entitled to recover the full amount from all other prior parties including the "accommodation" and the "accommodated" party.

The second rule provides for partial failure of consideration, which may again, either consist of money or other things than money, e.g. goods. Sec.

(*m*) *Sassoon & Sons v. International Banking Corporation*, 29 Bom. L.R. 1181.

44 provides that where the original consideration for a nego. inst. consists of money and it was either originally absent in part or has subsequently failed in part, the parties to the instrument standing in immediate relation can recover from each other, only the reduced amount and no more (see also Exc. 2 to sec. 43).

The third rule which is laid down by sec. 45 is that where the consideration which has partly failed consists of things other than money, e.g. goods, and the value of such failed consideration can be ascertained without a collateral inquiry, the parties standing in immediate relation can recover from each other only the proportionately reduced amount and not the whole amount of the bill.

The fourth rule which follows from the above is that where the consideration which has partly failed consists of things other than money and is such that its value cannot be ascertained without a collateral inquiry, the immediate parties to the bill are entitled to recover the full amount of the bill from each other, leaving the question of the value of the failed consideration to be decided by a separate suit in that behalf. The last two rules may be illustrated as follows: A draws a bill of exchange on B for Rs. 2,000 in favour of C (being the value of the goods supplied by A to B). B accepts the bill. It subsequently turns out that the goods are of inferior quality. If C sues B on the bill, B is bound to pay the whole amount of the bill to C. But if B dishonours the bill and A has to pay C, the question arises whether A can recover from B Rs. 2,000, i.e. the full amount of the accepted bill? The answer depends upon the nature of the failure. If the value of the part consideration which has failed can be speedily assessed in terms of money (e.g. where two bales having to be delivered, only one is delivered under the contract so that there is obviously a failure of one half of the consideration), B can take up the defence of such partial failure of consideration in A's suit against him for the full amount of the bill. But if the value of such part cannot be ascertained without an elaborate independent inquiry, B will have to pay the whole amount of the bill to A, his only course being to file another suit against A to recover back part of the amount paid by him, as on a failure of consideration.

Notice that under sec. 118(a), consideration is always presumed in favour of a holder of a negotiable instrument. The presumption however is rebuttable. Notice that inadequacy of consideration is not a ground to invalidate a nego. inst., just as it is not a ground in case of other contracts.

NEGOTIATION

Negotiation: what is: When a nego. inst. is transferred to any person so as to constitute that person the "holder" thereof, the instrument is held to be "negotiated" (sec. 14). It thus requires two conditions to be fulfilled: (i) there must be a transfer of the instrument to another person; (ii) the transfer must be made in such a manner as to constitute the transferee the holder of the instrument. Two special methods of transfer are prescribed by the Nego. Insts. Act for this purpose: (i) by endorsement and delivery in case of order instruments and (ii) by mere delivery, in case of "bearer instruments".

Negotiation and assignment distinguished

A pro. note, bill of exchange or cheque represents a debt. A debt, not secured by a mortgage, is called in law an "actionable claim". Just as a pro. note, bill of exchange or cheque and the debt represented thereby can be transferred by the method of "negotiation", as provided by the Nego. Insts. Act, they can also be transferred by a proper "assignment" thereof, according to certain rules laid down for transfer of "actionable claims" by the Transfer of Property Act.

Of the two methods of transfer, however, the one prescribed by the Nego. Insts. Act and recognised as valid by the "Law merchant" has manifest advantages over the other, as is clear from the following :

(i) "Negotiation" requires delivery only (i.e. endorsement and delivery) to effectuate a transfer; assignment requires a written document signed by the transferor (sec. 130, Trans. of Pro. Act).

(ii) In order to make an "assignment" of a debt complete and effective, notice of the transfer must be given by the transferee to the debtor; "negotiation" requires no such notice to be given in order to be effective.

(iii) On "assignment" the transferee of an "actionable claim" takes it subject to all the defects in the title of and subject to all the equities available against, the transferor. In case of 'negotiation', the transferee takes it free from all the above burdens, if he is a "holder in due course". This is the most important advantage.

(iv) Consideration is always presumed in case of nego. insts.; in case of "assignment", the onus lies on the transferee to prove consideration for the transfer.

Importance of delivery

Sec. 46 of the Act emphasizes a particularly important point with regard to nego. insts., viz. delivery. The sec. lays down that the making, acceptance or endorsement of a negotiable instrument is not complete till delivery thereof, whether actual or constructive. Further, as between parties standing in immediate relation, delivery must be made by the person making, accepting or endorsing the instrument or by his duly authorised agent. Thus a bill of exchange, drawn and signed by A on B in favour of "C or order", is not and cannot be regarded as a nego. inst. till A delivers the instrument to C. Similarly, if C endorses it to D, the indorsement is not complete, till C actually delivers the instrument so endorsed to D. In other words, delivery is an essential element in the making, endorsing or accepting of a nego. inst.

The delivery may be either actual or constructive. Thus if in the above illustration, C after endorsing the bill in favour of D, agrees to hold it as agent for D, there is in law sufficient delivery to D, though no actual delivery has been made by C to D. The delivery, further, must be absolute and unconditional. If a nego. inst. is delivered by a person to another conditionally or for a special purpose, property in the instrument does not pass to such person and he holds such instrument in law as trustee or agent of the transferor. Thus a cheque payable to bearer, handed over by the holder to a banker for collection, is not "delivered" to such banker so as to entitle him to further negotiate it as holder thereof. As sub-sec. (3) of sec. 46

points out, between parties to an instrument and any holder thereof (except a holder in due course), it can always be shown, if such be the case, that the instrument was delivered to such person, conditionally or for a special purpose. No absolute property in such instrument can, in such a case, vest in the person to whom it is so delivered. Notice that sending a cheque by post is not delivery to the addressee (n).

Negotiation—How effected

Negotiation can, generally, be effected in two ways: (i) a pro. note, cheque and a bill of exchange payable to bearer is negotiated by delivery thereof (sec. 47). The delivery may be either actual or constructive. The delivery however must be with the intention to negotiate. A delivery to another for safe keeping or as agent merely, will not amount to "negotiation" in law.

Delivery by way of negotiation may be either absolute and unconditional or may be conditional or for a special purpose, e.g. a transfer with a condition that the instrument shall not have effect until a certain event happens. In such a case the instrument is not negotiable till that event happens (sec. 47, cl. 2). The only exception is in favour of a "holder in due course" (ibid). A nego. inst. delivered by a holder to another with a condition that it is not to take effect unless a specified event happens is called an 'escrow'.

Notice that a transfer of a bearer instrument by a holder to another by delivery, does not involve the necessity of making an endorsement. The person taking it by such delivery, therefore, is not taking "under an endorsement". He is not an endorsee and the rules of liability applicable to endorser and endorsee, therefore, do not apply to such a case. The transaction is in fact regarded by law as a sale.

(ii) A pro. note, cheque or bill of exchange payable to order can be negotiated by the holder by endorsement and delivery thereof (sec. 48). Both the above conditions must be fulfilled before an order instrument can be negotiated. If an order instrument is negotiated by delivery only, without proper endorsement, the transferee will not take it as an endorsee, but will be regarded by law as an assignee of an actionable claim with a further right to insist that the transferor shall duly execute a proper endorsement thereon in his favour.

A third way of negotiating an instrument is by what is called "converting an endorsement in blank into an endorsement in full". Where the holder of a nego. inst. endorsed in blank, without writing his own name, writes above the endorser's signature, a direction to pay to any other person as indorsee, he is said to convert an "endorsement in blank into an endorsement in full". The holder, so acting, is not an indorser and is therefore not liable as such in law (sec. 49). Thus if B is holder of a bill drawn in favour of A or order on which A has made an indorsement in blank and if B adds the words 'pay C or order' above A's blank indorsement, and then hands over the bill to C, the bill is negotiated to C but C's indorser is not B but A, under whose full indorsement, C now holds the bill. B on the other hand escapes, by this means, all liability as "indorser".

Effect of indorsement and delivery

The legal effect of negotiation by endorsement and delivery is (i) to transfer property in the instrument from the indorser to the indorsee; (ii) to vest in the latter the right of further negotiation and (iii) a right also, to sue on the instrument in his own name, against all the other parties (see sec. 50).

Various kinds of indorsements

An indorsement may be either (i) "in blank" or (ii) "in full". It is "in blank", when the person making it signs his name only. It is "in full", when the person signing adds a direction to pay the amount to or to the order of a specified person (sec. 16). Full indorsement is also called a "special indorsement".

An indorsement may also be (i) absolute, (ii) restrictive or (iii) conditional. It is "*absolute*" when no conditions are attached to it, so as to make the indorsee's right against the endorser dependent on contingencies. It is "*restrictive*" when (i) by express words, it either restricts or excludes the indorsee's right to further negotiate the instrument or (ii) constitutes the indorsee merely an agent (a) to indorse the instrument or (b) to receive the contents for the indorser or another specified person (sec. 50). It is "*conditional*" when (i) by express words (a) it excludes the indorser's liability on the instrument or (b) makes such liability or the indorsee's right to receive amount of the instrument, dependent on the happening of a specified uncertain event (sec. 52).

Restrictive indorsement

An indorsee under a "restrictive indorsement" has no right to further negotiate the instrument. If he purports to do so, his transferee will have no right to enforce the instrument against any party thereto. A person taking under a restrictive indorsement, however, has the right to recover the amount of the same, though when recovered, he holds the amount as agent for the indorser. Similarly, he has also got the right to sue all the parties liable on the instrument in his own name. The law requires, however, that the words restricting negotiation must be absolutely clear. Thus it has been held that crossing a cheque, with the words "*account payee*" and mentioning a bank, is not restrictive indorsement so as to invalidate a further negotiation of the cheque by the indorsee. On the other hand, an indorsement like "pay to A B's account" or "to the credit of A, B, with C, D Bank" or "to be placed to the account of A, B with X Y Bank" or "to credit of my account", has been held to be good restrictive indorsement. An indorsement like "pay A" or "pay A value on account with B C", is not such. Notice that a restrictive indorsement may permit further negotiation for a special purpose. A further negotiation for such purpose will not then be invalid.

Conditional indorsement

A "conditional indorsement" does not affect the negotiability of the instrument, but only qualifies the duties and obligations of the indorser. Hence it is sometimes also called a "qualified indorsement". Such an indorsement may exclude the indorser's liability altogether, e.g. where an instrument is indorsed by A "*sans recourse*", i.e. "without recourse to A".

In such a case, though A will be an indorser, he will not be liable as such, in the event of the instrument being dishonoured. It may also make the indorser's liability conditional, e.g. "to pay A if a particular ship arrives within a year", or "to pay A, unless I give notice to the contrary". In such a case, the indorser's liability will only arise when the condition is satisfied. Of course, the indorsee, in such a case, retains the right to sue all the other prior parties, in spite of the condition not being fulfilled. This is otherwise, however, where the condition makes the indorsee's right to receive the amount, dependent upon a condition. In such a case the indorsee cannot sue any party on the bill, till the condition is satisfied. A peculiar situation sometimes arises in case of such conditional indorsements, particularly where the indorsement is "*sans recourse*". If A indorses a bill in favour of C and C in favour of D and D in favour of E and E thereafter again transfers the instrument by negotiation to A, the result of the whole operation is to make A liable as (original) indorser and also as (last) indorsee. In other words, the instrument has been "negotiated back", to the original holder. This is called "negotiation back" or "taking up a bill".

Negotiation back

When a bill is thus "negotiated back", three consequences follow : (i) no indorsement in favour of the original holder (A) is necessary when the bill is re-transferred by the last holder (E) to him ; (ii) A on receiving the instrument back, may cancel all the intervening indorsements, and (iii) A may re-negotiate the bill as if it contained no indorsements at all. The reason for the cancellation of the intervening indorsements is that to enforce them against each of the various indorsers (A to E) would involve a circuitry of action ; A having ultimately to sue himself as both indorser and indorsee. The point to notice is that such a result does not follow when the indorsement of A is "*sans recourse*", because in such a case A cannot be made liable as an indorser and can therefore very well sue as indorsee all previous indorsers on the bill (excepting himself) [See sec. 50, cl. (2)]

Fuculative indorsement

(iv) Another kind of indorsement is also possible, which is called a "*fuculative indorsement*". Under such indorsement, the indorser *enlarges* his liability as indorser, e.g. "pay A or order, notice of dishonour waived". In such a case, the indorser stipulates that he would be liable as an indorser, even though the holder fails to give him the necessary notice of dishonour of the bill as required by law.

Rules regarding indorsements

(i) A part of the amount of a bill cannot be indorsed. An indorsement in favour of A for Rs. 500 only out of a bill for Rs. 1,000 is invalid in law (sec. 56). The only exception is where a part of the amount of the bill has been paid or received by the holder. In such a case the bill can be indorsed for the balance (*ibid*).

(ii) An instrument originally payable to order, if indorsed in blank, becomes a bearer instrument except in the case of a crossed cheque (sec. 54).

(iii) If an instrument after being indorsed in blank, is by a subsequent holder indorsed in full, the indorser of such a full indorsement is liable for

the amount only to such indorsees who have taken under such full indorsement and persons deriving title through them (sec. 55). Notice that the sec. does not alter the rule that an instrument indorsed in blank remains a bearer instrument, though subsequently indorsed in full. Such an instrument therefore can still be validly transferred by mere delivery. The sec. purports to define the rights and obligations of a person taking under such a subsequent full endorsement only. Notice further that the marginal note to the sec. is incorrect.

(iv) The legal representatives of a deceased holder who had already indorsed an order bill before his death, cannot negotiate the bill by delivery merely (sec. 57). They must re-indorse the bill as such and then negotiate it by delivery.

(v) Indorsements are presumed to have been made in the order in which they appear (sec. 118) but the contrary can be proved.

Defendant signed two promissory notes payable on demand on specified dates to "F and F. N. Co. or order". The notes were endorsed by F. N. a partner in the payee firm (who had authority to endorse on behalf of the firm) in favour of the plaintiffs or order, with the words "F. & F. N.", the word "Co." being omitted. The plaintiffs (bankers) discounted the notes in good faith and without notice of any defect in the title of the payee. The notes being dishonoured, the plaintiff bank sued the defendant (the drawer of the notes), as holders in due course. *Held*, there being a patent defect in the endorsement, the notes could not be said to be complete and regular; the plaintiffs, therefore, could not claim as holders in due course, but they could sue the drawer as holders for value, because the endorsement, though irregular, was valid, so as to pass the property in the notes to the plaintiffs (o).

Notice that a person who makes an irregular endorsement is liable thereon in spite of the irregularity. Thus, if a payee who is wrongly described on the front of the bill endorses it in his true name, the endorsement is irregular but he is liable to any subsequent holder and cannot set up the irregularity as a defence. Similarly, a regular endorsement will not impose liability if it is forged or unauthorised. In other words, irregularity has to be distinguished from validity and from liability (*ibid*).

Who can negotiate: By law only a (i) maker, (ii) drawer, (iii) payee, or (iv) an indorsee can negotiate a bill unless negotiation is restricted. Where there are more such persons than one, all must join in making, drawing and indorsing the instrument. The above persons however must be in lawful possession of the instrument (sec. 51). Thus a person obtaining an instrument by theft or fraud cannot negotiate it, because he is not a "holder".

Negotiation: how far: A nego. inst. can be negotiated until payment or satisfaction thereof by the maker, drawee or acceptor at or after maturity (sec. 60). Thus it can be negotiated after maturity or even after dishonour (subject, in both cases, to certain disadvantages). If it is paid before maturity, by the acceptor, maker or drawee, it can still be negotiated by them. This is because such payment is not a "payment in due course". This is called "re-issuing a bill". If it is, however, paid or satisfied by the acceptor, drawee or maker, at or after maturity, it cannot be negotiated further, because the bill then becomes defunct (sec. 60).

Negotiation after maturity or dishonour: The holder of a bill after dishonour, with notice thereof, has no better title to the bill as against the

other parties, than the title of his transferor. The same is the rule with regard to a holder of a bill after maturity (sec. 52). In other words, in case of such holder, though the instrument remains "negotiable", i.e. capable of being transferred as cash, the distinguishing feature of a negotiable instrument, viz. that a transferee thereof for value without notice of a defect in title of his transferor gets a good title to the instrument, does not remain applicable. The only exception is in case of "accommodation notes or bills", as regards which sec. 59 specifically provides that the holder of such a bill, after maturity, in good faith and for consideration, can recover the amount from any prior party to the same.

Negotiation by unauthorised persons

A question of particular difficulty arises when a nego. inst., e.g. a bill of exchange or cheque, gets into the hands of an unauthorised person who thereupon proceeds to negotiate it, as if he were the lawful owner of the same. An instrument may get into unauthorised hands (i) because it is lost, (ii) by reason of being obtained from the lawful maker, acceptor or holder thereof by means of an offence or fraud or for an unlawful consideration or (iii) as a result or by reason of forgery. The law as regards each of the above cases is different and requires careful consideration.

Questions involved

Five important questions are involved in dealing with the above cases : (i) the 'rights', if any, of the unauthorised person ; (ii) the rights, if any, of persons taking through such an unauthorised person ; (iii) the rights of a "holder in due course" of such an instrument ; (iv) the rights of the true owner of the instrument ; and (v) the rights of the parties liable to pay with regard to such instrument.

The relevant secs. dealing with the above questions are sec. 58 and sec. 82(3) of the Act. Sec. 58 provides : "When a negotiable instrument has been lost or has been obtained from any maker, acceptor or holder thereof, by means of an offence or fraud or for an unlawful consideration, no possessor or indorsee who claims through the person who found or so obtained the instrument is entitled to receive the amount due thereon from such maker, acceptor or holder or from any party prior to such holder, unless such possessor or indorsee is, or some person through whom he claims was, a holder thereof in due course". Sec. 82, sub-sec. (3), provides "the maker, acceptor, or indorser respectively of a negotiable instrument is discharged from liability thereon, to all parties thereto, if the instrument is payable to bearer or has been indorsed in blank and such maker, acceptor, or indorser makes a payment in due course of the amount due thereon".

Considering the above secs. together, it is clear that (i) a person who gets hold of a negotiable instrument without a lawful title thereto has no right to enforce payment from the parties liable thereon (sec. 58); (ii) a "holder in due course" of such an instrument, however, can enforce it against all parties liable thereon ; (iii) the maker, drawee and acceptor of such an instrument (if payable to bearer or if indorsed in blank) would obtain a valid discharge, if he pays the amount thereof to the apparent "holder" by a payment in due course (sec. 82, cl. 3). (iv) The question of forgery has not been specifically dealt with or provided for by the Act.

Lost instrument

The law in each of the above cases may be more fully stated as follows : *Lost Instrument* : (i) The finder of a lost instrument gets no title to it nor persons do deriving title through him (with one exception), (ii) the finder cannot sue the acceptor or drawee thereon (sec. 58); (iii) the true owner can recover the instrument from him; (iv) if the finder negotiates the instrument (being a bearer instrument or one endorsed in blank), to a holder in due course, such holder gets a complete title to it (sec. 58). (v) If (being payable to bearer or being endorsed in blank), the maker, drawee or acceptor pays the amount of such instrument by a payment in due course to such unauthorised person, he gets a good discharge (sec. 82).

Bills obtained by offence, fraud or for unlawful consideration

The rules applicable in such cases are practically similar to those stated above, viz. (i) the person obtaining a nego. inst. by any of the above means, gets no title to it. (ii) He and those claiming through him (with one exception) cannot enforce payment thereof from the parties liable; (iii) A holder in due course however of such an instrument (if payable to bearer or indorsed in blank), is entitled to enforce payment; (iv) the parties liable on the bill (when payable to bearer or indorsed in blank) get a good discharge by payment in due course thereof.

Forgery

As stated above, the Act does not specifically deal with this subject. The law however is governed by two simple principles :

(i) A forged signature of the drawer or acceptor is in law wholly inoperative ;

(ii) a forged indorsement is regarded in law as no indorsement at all.

In both the cases, therefore, the instrument is regarded as incomplete on the face of it and no title, right or protection can be claimed to arise or result from any dealing with such an instrument.

Thus where *the signature of the drawer or acceptor is forged* : (i) the property in the instrument remains in the person who was the real owner thereof at the time of the forgery, (ii) the holder of the forged instrument cannot enforce it; (iii) he cannot give a valid discharge for it; (iv) if he obtains payment on such instrument, he cannot retain the same against the true owner; (v) the person paying the instrument can recover the amount paid from such person as payment under a mistake; (vi) the party liable on the instrument, cannot obtain a good discharge in respect of such instrument, even by a "payment in due course", to such unauthorised person. This is because sec. 58 and sec. 82(c) do not apply to such a case. (vii) A holder in due course also, of such an instrument, cannot get any protection as such, because the instrument is incomplete on the face of it.

Where *an indorsement is forged*, two cases arise for consideration : (a) of indorsement in blank and (b) of indorsement in full. In the first case, the bill becomes a bearer bill and the transferee of such a bill does not take *under an indorsement*. A forged indorsement in blank therefore does not necessarily affect the title of the transferee of such a bill. He can enforce payment of the bill, whether he is an ordinary holder or a holder in due course. In the second case, however, the indorsee of such a bill takes under

the indorsement and a forged indorsement being in law no indorsement, such indorsee would thus be taking an instrument which was incomplete on the face of it. Such indorsee, therefore, cannot enforce payment of the bill nor can a holder in due course thereof do the same. A payment made in respect of such a bill also, would not secure any protection to the drawee or acceptor, even if it be a "payment in due course". The drawee of such a bill remains liable on the bill to the true owner thereof notwithstanding such payment. Notice, in this connection that, under secs. 121 and 122, an acceptor and an indorser are precluded from denying to a holder in due course, the genuineness of the drawer's signature. The fact that forgery was caused or facilitated by the negligence of the acceptor, has been held in England not to be sufficient to hold him liable on a forged bill, even to a holder in due course (p).

Bankers and forgery

Bankers who deal with nego. insts. on behalf of their customers stand on a different footing with regard to the above matters. Their position in law may be stated as follows :

(i) Bankers paying or discounting bills of exchange which bear forged indorsements of their customers, enjoy no special protection in law, even though their payment is a payment in due course. A forged indorsement being no indorsement in law, bankers paying such bills are paying incomplete instruments and thus cannot obtain any discharge against their customers by such payment.

(ii) A special protection however is provided by sec. 85 for bankers who pay order cheques of their customers, on which the indorsement is forged. The sec. provides : "where a cheque payable to order purports to be indorsed by or on behalf of the payee, the drawee (banker), is discharged by a payment in due course".

(iii) Similarly, where a cheque is originally expressed to be payable to bearer, the drawee (banker) is discharged by payment in due course to the bearer thereof, notwithstanding any indorsement whether in blank or in full appearing thereon, and notwithstanding that any such indorsement purports to restrict or exclude further negotiation [sec. 85 (2)].

(iv) Further, where a draft drawn by one office of a bank on another office of the same bank, payable to order on demand, purports to be indorsed by or on behalf of the payee, the bank is discharged by a payment in due course (sec. 85A). Thus in case of cheques, or drafts payable to order, the banker who pays them by a payment in due course, enjoys protection at law, if it subsequently turns out that the payee's indorsement thereon was forged. Similarly, a banker paying an originally bearer cheque by a payment in due course to bearer is protected, notwithstanding that an indorsement thereon, whether in full or in blank, is forged and whether there are words therein restricting or prohibiting negotiation.

Notice however that sec. 85 only refers to the payee's indorsement as forged. Apparently a forged signature of an indorser will not be within the sec. Secondly, the forgery of a customer's signature on a cheque is also not within the sec. This is because of the well-known principle of banking law

which lays down that it is the banker's business to know his customer's genuine signature and distinguish it, at his peril, from his forged signature. A banker, therefore, paying a cheque, on which the drawer's signature is forged is not protected and he is not entitled to debit such payment to his customer's account.

The customer, however, has also some duties cast upon him by law in this matter. Firstly, the forgery must not have been the result of his own negligence. Thus if his own drafting of the cheque is so negligent that a forgery can easily take place, e.g. if he leaves blank spaces before figures and words, he cannot blame the banker for such payment but must himself bear the loss. Further, he is bound in law to inform the banker about such unauthorised withdrawals, immediately on coming to know of the same. If he fails in his duty, he cannot hold the banker liable for such payment. Notice that a banker enjoys protection, only with respect to a payment in due course, i.e. with due care and caution. Notice further that the protection is with reference to forged as well as unauthorised indorsements. Lastly, it has been held in England that carelessness on the part of the customer in not locking up his cheque book is not "negligence" on his part, as understood by law (q).

PRESENTMENT

Before payment could be obtained in respect of a nego. inst., it must, in certain cases, be "presented" to the party liable, i.e. a demand must be made on him, after showing the instrument, to pay the amount of the instrument. The questions to whom and by whom and when and how such "presentment" is to be made and the consequences of non-presentment form the subject-matter of this section. Presentment is of two kinds: (i) for acceptance and (ii) for payment.

Presentment for acceptance

This is not necessary (i) in case of bills payable on demand; (ii) bills payable within a certain number of days after date and (iii) bills payable on a certain day. Presentment for acceptance is optional in such cases. The parties who have already put their signatures on the bill are liable thereon without such bills being presented for acceptance. Presentment for acceptance is, by law, *necessary* (i) where the bill is payable a specified time after sight (to fix its maturity); and (ii) where the bill expressly stipulates for such acceptance (sec. 61). Even in cases where presentment for acceptance is optional, it is always advisable to present the bill for acceptance, for two reasons: (i) because thereby additional security, i.e. of the acceptor is obtained; (ii) further, if the drawee refuses to accept, recourse can be had at once against the parties liable as on a dishonour.

Presentment to whom and by whom: The bill must be presented to (i) the drawee or his authorised agent, if he can be found after reasonable search (sec. 61); if he cannot be found, the instrument is treated as dishonoured (sec. 75); (ii) to all the drawees, unless they are partners or agents; (iii) to the legal representatives of the drawee, if the latter be dead and (iv) to the Official Assignee or official receiver, if the drawee is insolvent. The bill must be presented by a person entitled to demand acceptance (sec. 61).

Presentment when, where and how: Presentment for acceptance must be made within a reasonable time after the instrument is drawn, during business hours, on business day and if a place is specified, at that place. If at such a place the drawee is not found after reasonable search, the bill can be treated as dishonoured (sec. 61). When authorised by agreement or custom, presentment through post office by registered letter is sufficient (sec. 61).

Effect of non-presentment for acceptance: Where such presentment is obligatory by law, non-presentation of the bill has the effect of discharging all parties to the bill (including the drawer and the indorser, if any) from their liability (sec. 61). Presentment for acceptance is excused if (i) the drawee or his authorised agent cannot after reasonable search be found (sec. 61); and (ii) if the drawee is a fictitious person or a person incompetent to contract (sec. 91).

Drawees' time for deliberation: If the drawee so requires, the holder must allow the drawee, 48 hours (exclusive of public holidays) to consider whether he will accept the bill (sec. 61). This is called "drawee's time for deliberation". The instrument, therefore, cannot be treated as dishonoured by non-acceptance, till such period has elapsed. Delay in presentment is excused if caused by circumstances beyond the control of the holder, and is not attributable to his default, misconduct or negligence, but in such cases, presentment must be made within a reasonable time after the cause of the delay has ceased to operate (sec. 75A).

Presentment for payment

Presentment for payment is excused in the following cases: (i) if drawee intentionally prevents presentment of the instrument, or closes his place of business (the bill being payable at such place), or if after reasonable search, he or his authorised agent is not found at all or not found at the place where the bill is specified to be payable; (ii) if presentment for payment is waived, e.g. (a) by a party expressly agreeing to be liable in spite of non-presentment; (b) by a party after maturity making a part payment or promising to pay the amount of the instrument or otherwise impliedly waiving his right of presentment, with notice of non-presentment, as against such party; (iii) as against the drawer, when the drawer could not suffer damage on account of non-presentment, e.g. in case of the accommodation bill (sec. 76).

Effects of non-presentment for payment

(i) Presentment for payment by the holder is not necessary in law in order to charge the drawee or acceptor of a bill payable on demand (sec. 64). This is because these parties are already liable on the bill and the general rule of law is that the debtor must find the creditor within the realm and pay the amount due to him. Presentment for payment, however, in such a case, is necessary in order to charge the *other parties* liable on the bill, e.g. the drawer or endorser (sec. 64). If no presentment is made, these parties are not liable on the bill (*ibid*). (ii) As regards bills payable at a specified period after date or after sight, these must be presented for payment at maturity (sec. 64). If not so presented, *no party* would be liable on the bill.

Presentment: how made: Where authorised by agreement or custom, presentment through post office by registered letter is sufficient (sec. 64).

It must be made by the holder or a person authorised on his behalf (sec. 64). It must be made to the drawee, or his authorised agent or to all the drawees, if more than one, to the legal representatives of the drawee, if he is dead and to the Official Assignee or receiver of the drawee, if he is insolvent (sec. 75). It must be made during usual business hours and if payable at a bank, during the usual banking hours (sec. 65).

Place of Presentment: (i) If a bill is made or accepted "at a specified place and not elsewhere", it must be presented at that place for payment. If not presented at that place, no party will be liable on the instrument (sec. 68). (ii) If a bill is drawn or accepted at a specified place, it must be presented for payment at that place in order to charge the drawer thereof (sec. 69). (iii) Where no place for presentment is specified, it must be presented at the place of business (if any) of the acceptor or his usual place of residence (sec. 70). (iv) Where the acceptor has no fixed place of business or residence, the bill must be presented to the acceptor wherever he can be found (sec. 71).

Where a nego. ins. is payable at a particular place, e.g. "within the Bank of India", it must be presented at such place, in order to charge the acceptor, provided, of course, the acceptor is present there (q1).

Time of presentment: As regards bills payable on demand, they must be presented within a reasonable time after they are received by their holder (sec. 74).

Delay in presentment: If delay is caused by circumstances beyond the control of the holder and not through his default, negligence or misconduct, it will be excused, provided the bill is presented within a reasonable time after the cause of the delay has ceased (sec. 75A).

PAYMENT OF BILLS

Payment: In order to discharge the acceptor, payment of a bill must be made to the "holder" of the instrument (sec. 78) or to the person lawfully entitled to receive the payment. This is, however, subject to the rule contained in sec. 82, cl. (c), which provides that where an instrument is payable to bearer or is indorsed *a blank* a payment in due course by the acceptor or indorser thereof, of the amount due thereon, gives a complete discharge to all parties liable on the bill. "Payment in due course" means "payment in accordance with the apparent tenor of the instrument, in good faith and without negligence, to the person in possession of the bill, under circumstances which afford no reasonable ground for suspicion that the person is not entitled to receive such payment" (sec. 10).

Reading the two secs. together, it is clear that in case of a bearer instrument, a payment in due course, by the maker, acceptor or indorser of such instrument, to the person in possession thereof, gives a complete discharge to all parties thereto, whether the person who is paid is the lawful holder of the instrument or otherwise. This leaves the case of order instrument untouched. The rules with regard to such instrument with particular reference to forgery, have already been discussed (see ante). Notice that payment in order to discharge the acceptor must be made by or on behalf of the acceptor. Thus a payment by the drawer or endorser of the bill does not discharge the acceptor. The payment also must be at or after maturity.

Interest: Two rules are laid down by the Act in this connection : (i) If the instrument mentions the rate of interest, it is payable at that rate, till tender or realisation of the amount and if a suit is filed, until such date after suit as the Court directs (sec. 79). (ii) If the instrument is silent on the point, interest is payable at 6 per cent per annum from the date fixed in the instrument (in case of an indorser, from the date the notice of dishonour reaches him), until tender or realisation or till such date after suit as the Court may direct (sec. 80).

As regards the first rule, the Usurious Loans Act of 1918, where applicable, will have the effect of controlling the amount recoverable by way of interest. As regards the second rule, notice that as the sec. provides, no oral or written agreement between the parties as regards interest, can be proved, where the rule applies. Notice that under sec. 77, where a bill is presented to a banker for payment as provided by the instrument, the banker is a bailee of the same and is liable to the holder for loss or damage caused to him by his negligence or want of care to the bill. Secondly, the acceptor, before payment, is entitled to be shown the bill and after payment is entitled to have the bill delivered up to him. If it is lost, an indemnity must be given to him in respect thereof (sec. 81).

DISCHARGE OF BILLS

Discharge: A nego. inst. may be discharged in either of two ways : (i) by being completely extinguished as such instrument and thereby releasing all parties who are liable on the instrument ; (ii) by discharging some parties only from their liability thereon.

Complete discharge

A nego. inst. is completely discharged when the acceptor or maker thereof pays the amount of the instrument to the person lawfully entitled to receive it. After such payment the instrument becomes extinguished and cannot be negotiated any further, not even to a holder in due course. Notice in this connection, that it is only the acceptor or the maker (of a promissory note) alone, who can make such payment, with the above effect. Neither the drawer nor the endorser can, by such payment, extinguish the instrument.

Discharge as regards parties

A nego. inst. may be discharged, as regards some parties thereto, in the following ways : The maker, acceptor or endorser of a nego. inst. is discharged from liability thereon (i) to a holder, who cancels the name or names of the above parties or any of them with intent to discharge him or them from liability thereon ; (ii) to a holder who otherwise discharges the above parties or any one of them, and to all persons claiming under such holder, after notice of such discharge ; (iii) to all parties to the instrument if a bearer instrument (i.e. one originally bearer or indorsed in blank) is paid by any one of the above parties, by a payment in due course (sec. 82). (iv) When the holder of a bill allows more than 48 hours to the drawee to consider whether he will accept the bill or not, all previous parties to the bill, not consenting to such extension, are discharged (sec. 85). (v) Where the holder acquiesces to a qualified acceptance of a bill, all prior parties, not consenting to such qualified acceptance are discharged (sec. 84). (vi) Where a nego. inst. is materially altered, the instrument is void against all persons

who are parties thereto and who have not consented to such alteration, unless such alteration was in order to carry out the common intention of the original parties. If such an alteration is made by an indorsee, it discharges his indorser from all liability in respect of the consideration for the instrument also (sec. 8). (vii) By the bill, at or before maturity, being held by the acceptor in his own right, all the rights of action therein are extinguished (sec. 90).

As regards (i), notice that cancellation through inadvertence or mistake, does not discharge the party whose name is cancelled on the bill. The cancellation must also clearly appear on the bill.

As regards (ii), it covers all cases of release from liability by means of an agreement between the parties concerned, e.g. accepting another bill in satisfaction of the existing bill. Notice that extension of time by consent of the parties does not operate as a release or cancellation of the original bill (r).

As regards (iii), the matter has been already discussed (see ante).

As regards (v), notice that an *acceptance is qualified* if (i) it is conditional, e.g. "accepted, payable on amount being realised from"; (ii) if it is partial as to the amount; (iii) if it substitutes a different time for payment; (iv) or a different place for payment, e.g. no place being specified, it undertakes to pay at a specified place and not elsewhere, or instead of the place specified, it undertakes to pay at another place and not elsewhere; (v) if it is not signed by all the drawees, unless they are partners (sec. 86). A holder is not entitled in law to accept such qualified acceptance. He is bound to treat the bill as dishonoured on such qualified acceptance by the drawee and proceed further accordingly. If he fails to do so and accepts such qualified acceptance, all previous parties to the bill, unless their consent has been obtained by him to such acceptance, will be thereby discharged.

As regards (vi), a *material alteration* is an alteration which either (i) changes the operation of the instrument or (ii) alters the liabilities of parties to such instrument. Thus alteration of the date, or name or time or place of payment or rate of interest, are material alterations. Similarly, addition of new parties to an instrument also amounts to a material alteration. On the other hand, an alteration which corrects a mistake, or which is made to carry out the original intention of the parties or which is made with consent, does not render the instrument void. Similarly, as the sec. itself provides, the making up of an inchoate bill (sec. 20), indorsing a bill (sec. 87), making conditional acceptance (sec. 86), and the crossing of an uncrossed cheque (sec. 125), are not material alterations. Notice that where a nego. inst. is materially altered without consent, no suit can be filed on the original consideration as well. A nego. inst. which is materially altered is in law regarded as a new instrument and would therefore require a new stamp.

In certain cases, parties may be estopped from relying on such alteration, in order to escape their liability thereon. Thus under sec. 88, an acceptor or indorsee of a nego. inst. is bound by his acceptance or indorsement, notwithstanding previous alteration of the same. Similarly, under sec. 89, where a promissory note, bill of exchange or cheque has been mate-

rially altered but does not appear to be so altered and where a cheque at the time of presentation does not appear to have been crossed, payment thereof by the person liable or the banker, according to the apparent tenor thereof, by a payment in due course, discharges the person or the banker from liability, and such payment cannot be questioned by the drawer or maker on the ground that the instrument was altered or the cheque crossed.

As regards (vii), notice that though sec. 90 refers only to bills, the same principle also applies to promissory notes also.

DISHONOUR, NOTING AND PROTESTING

Dishonour

A bill may be dishonoured in either of two ways : (a) by non-acceptance or (b) by non-payment.

A bill is *dishonoured by non-acceptance* when (i) it is not accepted by the drawee or all the drawees on presentment; (ii) when presentment being excused, the bill is not accepted, (iii) when the drawee is incompetent to contract, or (iv) when the acceptance is qualified (sec. 91).

A bill is *dishonoured by non-payment* when (i) the maker, drawer or acceptor makes default in payment on being duly required to pay (sec. 92) and (ii) when presentment for payment being excused, the bill remains unpaid at or after maturity (sec. 76). Notice that a dishonour of a bill by non-acceptance gives an immediate cause of action against the drawer and it is not necessary for the time for payment to arrive, to enable the holder to file a suit on the bill against the drawer (s).

An endorsement on a cheque by a drawee bank that it would pay on collection of drawer's assets has been held not to amount to dishonour (t).

Notice of dishonour

Before any rights can accrue to a holder in respect of a dishonoured bill (whether by non-acceptance or non-payment), it is essential that he should give due notice of dishonour as required by law to all parties whom he wants to hold liable on the bill. This is provided by sec. 93.

Notice of dishonour must be given (i) by the holder or some party who remains liable on the bill; (ii) it must be given to all parties whom it is sought to make liable. Thus if notice is given to the immediate indorser, he alone will be liable; though he may, in turn, give another notice to his immediate endorser and so on, along the whole chain. Generally, it is given to the drawer and thus it enures for the benefit of all parties deriving title from him, i.e. all intervening indorsers. (iii) Notice of dishonour however is not necessary to make the maker of the promissory note and the drawee or acceptor of a bill of exchange or cheque liable, because these parties are already aware of the fact of dishonour, being themselves the authors thereof. (iv) Further, notice to one of several parties jointly liable on a bill is in law sufficient notice to all.

Rules as to notice : (i) It may be given to the party himself or to his duly authorised agent. If the party is dead, it must be given to his legal

(s) *Ram Ravji v. Prahladdas*, 20 Bom. 133.

(t) *Silchar Bank v. Pioneer Bank Ltd.*, A.I.R. (1951) Assam 127.

representative (sec. 94). Notice in this connection that where the party despatching a notice to another is ignorant of the death of that other, the notice is not vitiated thereby (sec. 97). If the party is insolvent, the notice must be given to his official assignee or receiver.

(ii) It may be either oral or written. It may be in any form but it must contain the following particulars either expressly or impliedly, e.g.

(a) that the instrument has been dishonoured; (b) in what way, and (c) that the party to whom notice is given will be held liable thereon.

(iii) It must be given within a reasonable time after dishonour. If the instrument is dishonoured in the hands of an agent for presentment, he is entitled at the same time to give notice to his principal as if he were himself the holder, the principal in his turn being entitled to further period for giving notice of dishonour (sec. 96). A party receiving notice of dishonour is entitled to a reasonable time in order to give a notice to his prior party (sec. 95). In determining what is reasonable time, regard has to be had to the nature of the instrument and the usual course of dealings between the parties. Public holidays are to be excluded (sec. 105). If the holder and the party to be notified, live or carry on business in different places, notice despatched by the next post, or on the day next after the dishonour, is reasonable notice (sec. 106). If the parties live or carry on business at the same place, notice despatched so as to reach the party notified the day after the dishonour, is despatched within a reasonable time (*ibid*). The party receiving notice is governed by the same principles as regards transmitting the notice to his prior party (sec. 107).

(iv) The notice may be served personally or by post. If a notice duly despatched by post miscarries, it does not render the notice invalid (sec. 94).

(v) It must be given at the place of business of the party sought to be made liable and if he has no place of business, at his residence (*ibid*).

Effect of absence of notice: Where notice of dishonour is required by law to be given, a failure to give such notice has the effect of discharging the party entitled thereto from all liability on the instrument. Thus a drawer and an indorser to whom due notice of dishonour is not given when required by law, are discharged from all liability on the bill. This is because under secs. 30 and 35 respectively, the liability of both the drawer and the indorser is conditional on their receiving due notice of dishonour from the holder seeking to hold them liable. Notice that where a party who is liable on a bill is discharged therefrom by reason of absence of due notice of dishonour, no suit can be filed against him even on the original consideration (*u*).

Notice not necessary: Notice of dishonour, however, is not necessary in the following cases: (i) when it is dispensed with by the party entitled thereto; (ii) where drawer has countermanded payment, to charge the drawer; (iii) where the party charged would not suffer damage by absence of notice, e.g. in case of accommodation bill; (iv) if the party entitled to notice is not found or where the party bound to give notice cannot give notice through no fault of his, e.g. by death or illness; (v) where the drawer and acceptor are the same; (vi) where the party entitled to notice, with full knowledge of the facts, unconditionally agrees to pay the amount; (vii) in case of a promissory note, which is not negotiable (sec. 98).

Noting and protesting

Noting and protesting of a bill for dishonour are quite different from the "notice of dishonour" which has been considered so far. "Noting" means the proper authentication by a Notary Public of the fact of the dishonour of a bill. "Protesting" means a formal certificate signed by a Notary Public, setting out all the material facts relating to a particular dishonour of a bill. Neither "noting" nor "protesting" is compulsory by law so far as inland bills are concerned. They are purely voluntary and do not by reason of their absence, make a dishonour less a dishonour. Their object is to secure full evidence of the fact of dishonour of an instrument. Further, under sec. 119, where a bill is protested, the Court will presume the fact of dishonour, until the contrary is proved.

Noting: Where a promissory note or a bill of exchange has been dishonoured, either by non-acceptance or non-payment, the holder may cause the dishonour to be noted by a notary public on the instrument itself or on a paper attached therewith or on both. Such noting must be made within a reasonable time after dishonour and must contain the following particulars: (i) the date of dishonour; (ii) the reason, if assigned, for dishonour; (iii) if no reason is assigned, why the instrument is treated as dishonoured and (iv) the noting charges (sec. 99).

Protest: "Protest" is a formally drawn up certificate of the dishonour, signed by a notary public. A "protest" may be made for two purposes (i) for dishonour (by non-acceptance or non-payment) and (ii) for "better security". As regards the latter, sec. 100 provides that where the acceptor of a bill becomes insolvent or where his credit is publicly challenged before maturity, the holder may, within a reasonable time, cause a notary public to demand better security for the payment of the bill at maturity by the acceptor. If such security is refused, he can, within a reasonable time, cause the bill to be "protested for better security" by the notary public. Notice that where a bill is "protested for better security", it is not tantamount to a dishonour of the bill. The holder has still to wait, till the time for payment arrives, when, if the amount is not paid, he can proceed as on dishonour of the bill.

A protest must contain: (i) the instrument itself or a literal transcript thereof, including anything written or printed thereon; (ii) the name of the person for and against whom the instrument is protested. (iii) Statement as to demand for payment or acceptance or better security made by the notary public on the person concerned, the answer (if any) given by such person, or the fact that no answer was given or that he could not be found; (iv) the fact that the bill has been dishonoured, the time and place of dishonour and in case of better security, the time and place of the refusal thereof; (v) the signature of the notary public; (vi) the name of the acceptor for honour or person making payment for honour (if any) and the name of the person for whom and the manner in which such acceptance or payment was offered and effected (sec. 101).

Notice that under sec. 104, foreign bills, which are required by the foreign law to be protested, must be protested for dishonour as above, before rights in respect of such bills can accrue to parties thereto. Further, where a bill is required by law to be protested, notice of protest may be given by the notary public in place of notice of dishonour and such notice will in law

be equally effective (sec. 102). Where a bill of exchange is payable at a place other than the place at which the drawee resides and the bill is dishonoured by non-acceptance, it may be protested at the place specified, without presenting it to the drawee for payment, unless paid before or at maturity (sec. 103). Lastly, where a bill is required to be protested under the Act within a specified time, it is sufficient if it is "noted for protest", within such time; the actual drawing up of the "protest" may take place later (sec. 104A).

Notary Public.—Notice that by the Notarial Act (53 of 1952) the power is now taken by the Central Government and State Governments of India to appoint proper persons to act as Notaries Public. Their functions also are defined by the Act. These include (1) the power to present a promissory note, bill of exchange or Hundi for acceptance or payment or for better security and to note and protest the dishonour by non-acceptance or non-payment of a promissory note, bill of exchange or Hundi or protest for better security, to prepare acts of honour under the Neg. Inst. Act and to serve notice of such note or protest. Certificates are issued to the proper persons by the relevant Government to practise as such Notaries Public and Registers of their names are to be maintained. Before the Act was passed, Notaries Public were being appointed by the Master of Faculties in England.

Compensation: Where a bill of exchange is dishonoured by the drawee, the holder is entitled to recover compensation from all other parties to the bill who are liable thereon, as on a breach of contract.

Rules for such compensation are laid down by sec. 117. These are: (i) the holder is entitled to recover the amount due on the instrument, together with the proper expenses of noting or protesting; (ii) if the parties stay at different places, the sum so payable is to be calculated at the current rate of exchange (called "re-exchange"), (iii) if an indorser is made to pay the amount, he can recover the same from the party liable, with interest at 6 per cent from the date of payment till tender or realisation, together with all expenses caused by dishonour and payment, at the current rate of exchange if the parties reside at different places; (iv) the party entitled to compensation as above, may draw a bill on the party liable to compensate, payable at sight or demand, for the amount payable, together with all proper expenses incurred. If such bill (called a "re-draft") is dishonoured, the party dishonouring is liable on such bill in the same way as in the case of the original bill. The "re-draft" must be accompanied by the dishonoured bill with the protest if any. Notice that such compensation is in law regarded as liquidated damages, so as to enable the holder to file a summary suit in respect thereof under O. 37, r. 1, of the Civil Procedure Code.

SPECIAL RULES OF EVIDENCE: Secs. 118-121 of the Act lay down certain rules of evidence which are specially applicable to negotiable instruments. These rules have been evolved mainly by the Law Merchant and have been given legislative sanction by the above secs.

Presumptions: Certain presumptions are laid down by secs. 118-119 with regard to the negotiable instruments. Owing to these presumptions certain facts need not be proved unless the contrary is established. They are:

- (1) that every negotiable instrument was made, drawn, accepted, negotiated and transferred for consideration. This presumption prevails if the defendant fails to prove want of consideration;
- (2) that every negotiable instrument was drawn or made on the date it bears;
- (3) that every accepted bill was accepted within a reasonable time and before maturity;
- (4) that every transfer of a negotiable instrument was made before maturity;

- (5) that the endorsements on a negotiable instrument were made in the order in which they appear ;
- (6) that a lost negotiable instrument was duly stamped ;
- (7) that every holder of a negotiable instrument is a holder in due course, except when the instrument has been obtained from the true owner or from the lawful custodian or maker or acceptor thereof by means of an offence or fraud or for an unlawful consideration ; and
- (8) that a negotiable instrument has been dishonoured, if it is protested for dishonour.

Estoppels: Certain estoppels in law are also created by secs. 120-122 of the Act. By reason of these, certain persons are prevented from denying certain facts with regard to negotiable instruments dealt with by them. These are :

- (1) In a suit by a holder in due course, no maker of a promissory note or drawer of a bill of exchange or cheque or acceptor for honour of the drawer of a bill of exchange can deny that the instrument was valid as originally drawn or made (sec. 120).
- (2) In a suit by a holder in due course, no maker of a promissory note or acceptor of a bill of exchange payable to order can deny the payee's capacity, at the date of the note or bill, to endorse the same (sec. 121).
- (3) In a suit by a subsequent holder, no endorser can deny the signature or capacity of any prior party to the instrument (sec. 122).

These special rules have been noted earlier at their proper places.

International Law: As a result of worldwide circulation of bills of exchange and cheques as medium of commerce, questions often arise as to what law should be applied to them in a given case.

The Act under secs. 134-137 lays down certain rules on these points : (i) Unless the parties otherwise contract, the liability of the drawer or maker of a foreign bill of exchange, pro-note or cheque, is governed by the law of the place where the instrument was made ; (ii) the liability of the acceptor or endorser, in such cases, is determined by the law of the place where the instrument is payable (sec. 134) ; (iii) As regards what constitutes dishonour, or what is a reasonable notice of dishonour, the law of the place where the instrument is made payable, will determine the same, where the instrument is payable at a place different from that where it was made or indorsed (sec. 135). (iv) If an instrument is made, drawn, accepted or endorsed abroad, but it is in accordance with the law of India, any subsequent acceptance or indorsement thereon, in India, will not be regarded as invalid, because the agreement as evidenced by such an instrument, is invalid according to the law of such foreign country (sec. 136). (v) The law of a foreign country is generally presumed to be the same as Indian law till the contrary is proved (sec. 137).

CHEQUES

Cheques defined and distinguished: A "cheque" is defined by sec. 6 as "a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand". In other words, it is a bill of exchange drawn on a banker which is payable on demand. The general law of bills of exchange will therefore apply to cheques also. A cheque however is a peculiar type of negotiable instrument which resembles a bill of exchange in many particulars but does not so resemble in many others. Thus (i) a cheque does not require acceptance. (ii) It is not intended for circulation (iii) but for immediate payment. (iv) It is not entitled to any days of grace.

(v) It is always drawn on a banker. (vi) It is payable to bearer on demand, (unless crossed).

A banker holds the customers' moneys on a contract that the banker will allow the customer to draw on the same by means of cheques or drafts payable on demand, provided the amount to the credit of the account is sufficient to cover the demand. The banker is not a trustee of the moneys for the customer, the relation between them being that of a debtor and a creditor for the amount deposited by the customer and still remaining unpaid.

A cheque is an exception to the general rule that a bill of exchange cannot be drawn, "payable to bearer on demand" (sec. 31, Reserve Bank Act). Every person, who is competent to contract, can draw, indorse or pay a cheque. A minor, however, by doing so, binds all parties except himself (sec. 26). A minor can of course sue all other parties on a cheque in his favour (w).

Varieties of cheques

A "*bearer cheque*" is a cheque which is either (a) expressed to be so payable or (b) on which the last or only endorsement is an indorsement in blank (sec. 13). In England a cheque drawn in favour of a payee who is a fictitious or non-existing person is treated as payable to bearer (x).

"*Order cheque*" is a cheque (a) which is expressed to be so payable or (b) which is expressed to be payable to a particular person, without containing words prohibiting transfer or indicating that it shall not be transferable or (c) which is expressed to be payable to the order of a certain person (sec. 13).

"*Open cheques*": These are cheques which can be presented to the banker on whom they are drawn and paid by them "over the counter". There being always a great danger of such cheques being stolen or lost, the commercial community invented the method of "crossing cheques".

Crossing

"*Crossing*" is a device adopted by the mercantile community and sanctioned by law, which has the effect of making cheques payable to a bank only or to a particular bank in an account with such bank. Thus payment of a cheque is secured to a banker only. Crossing is of two types. *General crossing* consists of drawing two parallel transverse lines, across the face of a cheque, either with or without the words "not negotiable" and/or the words 'and Co.' in between (sec. 123). If in addition to general crossing, the name of a specified banker to whom the cheque is to be payable, is also written on the face of the instrument, with or without the words "not negotiable", it is called a "*special crossing*" (sec. 124).

Crossed cheques

Four rules are laid down with regard to crossed cheques: (a) Uncrossed cheques can be crossed by the holder; (b) a cheque crossed generally, may be crossed specially by the holder. (c) The banker to whom

(v) *Tarmahomad v. Tyeb*, 51 Bom. L.R.

(w) *Warick v. Bruce* (1813), 2 M. & S.

205.

(x) *South Ins. Corp. v. National Prov. Bank* (1936), 1 K.B. 328.

the cheque is specially crossed, may re-cross it specially but *only to another banker as his agent for collection*. (d) The holder may add the words 'not negotiable' on a cheque (secs. 125-127). The effect of adding the last words on a cheque, is not to invalidate a further transfer of the cheque, but to give the transferee of such a cheque, only such title thereto as the transferor had (sec. 130). As regards (c) above, the effect of the rule is to make a cheque specially crossed, twice over, unavailable as a medium of commerce. The second banker can only use the cheque, as an agent of the first banker, to collect the money on his behalf.

A "*post-dated cheque*" is a cheque payable on a different date than that on which it is actually drawn, the former date being placed on the cheque as the date of drawing. Such cheques are not illegal. They can be sued upon at maturity, notwithstanding the Stamp Act and may be negotiated to a holder in due course before maturity (y).

Marked cheques

A "*marked cheque*" means a cheque which is "marked" or certified by the banker on whom it is drawn, to the effect that it would be honoured when presented for payment. In a recent case (z) the Privy Council held that "certification of a cheque" was not equivalent to an acceptance of the cheque by the banker, so as to make the latter liable as on an accepted bill of exchange. In this case a cheque drawn on the Baroda Bank on 13th June, post-dated to 20th June, was certified by the manager of the bank "marked good for payment on 20th-6-39". The Punjab National Bank became holders in due course of the cheque, which being presented to the Baroda Bank for payment on the 20th June, was dishonoured on account of funds being insufficient. *Held*, the Baroda Bank was not liable on the cheque.

A cheque may be marked in a variety of ways. Sometimes the words "approved" or "good" are written on the cheque. Sometimes the drawee banker simply initials the cheque. Such cheques are also called "certified" cheques. The "marking" may be at the instance of the customer. In such a case it is presumed that if the customer, subsequently countermands payment, he would be liable to make good any damages which the banker may have to pay to a subsequent holder of the cheque who has taken it on the faith of such "marking". Bankers sometimes "mark" cheques *inter se*. By custom of bankers this is regarded as a promise by one banker to the other to pay the cheque. The legal validity of the custom however is doubtful. Sometimes the holder gets the cheque "marked" by the drawee banker. This only means that the banker *then* has sufficient funds to meet the cheque. It does not constitute the banker an acceptor of the cheque.

Liability of parties

In law, the drawee of a cheque is not liable as a principal debtor, but only the drawer is liable as such. The drawer stands in the position of an "acceptor" of a bill of exchange, the payee being in the position of "holder". The payee of a cheque has thus no cause of action against the drawee thereof, though he has against the drawer, on a breach of contract, if the cheque is dishonoured. The drawer may also have a cause of action against the drawee of a cheque, if having sufficient funds, the latter wrongfully fails to pay

(y) *Motilal v. Jagmohandas*, 6 Bom. L.R.

(z) *Bank of Baroda v. Punjab National Bank* (1944), A.C. 176.

the amount of the cheque (sec. 37). The action would be for breach of contract as also for damages for loss of reputation, if the dishonour has caused injury to the customer's credit. Notice that the liability of a banker however does not arise till a proper demand by the customer is made at the office where the customer's account is kept (a). In England a cheque drawn in favour of a payee who is a fictitious or non-existing person is treated as payable to bearer (al).

Payment of cheques

This question becomes important when the drawee Bank becomes bankrupt before the cheque is actually presented to it for payment.

(i) As between the holder and the banker, a cheque must be presented to the latter for payment, without unreasonable delay. A delay of 6 months will justify a banker in refusing to pay a cheque (called a "*stale cheque*").

(ii) As between the payee and the drawer, a cheque must be presented to the banker for payment within a reasonable time after issue and before the relations between the drawer and the banker have altered to the prejudice of the drawer (sec. 84). If the delay causes prejudice to the drawer as stated above, the drawer is discharged on the cheque to the extent of the prejudice so caused, the payee's right being to rank as a creditor of the bank for such amount (ibid). Thus if A had a credit of Rs. 10,000, with B, a banker, on 1st September 1947, and a cheque given by A to C for Rs. 5,000 on the 2nd September, is not presented by C to B till 30th September, but B has in the meanwhile become insolvent on 10th September, the result will be that to the extent that B's intervening insolvency causes damage to A, the latter will be discharged from his liability to C on the cheque. Thus if B's estate in insolvency pays only 8 annas in a rupee, C can recover Rs. 2,500 on the cheque against A and for the balance of Rs. 2,500, he will have to rank as a creditor of B's estate in insolvency (b).

(iii) As between the drawer and other parties, e.g. subsequent indorsees, the cheque must have been presented by them to the banker, within a reasonable time after their receiving it. What is reasonable time, is, in each case, a question of fact.

Discharge of banker

(i) With regard to "*bearer cheques*", a banker gets a good discharge, by payment in due course of the amount thereof to the holder of the instrument (sec. 78). It does not matter in law, if the apparent holder is not legally entitled to recover the payment [sec. 85(2)]. Where a cheque is originally payable to bearer, the drawee banker is discharged by payment in due course, of the amount to the bearer thereof, notwithstanding any indorsement in blank or in full thereon and notwithstanding restraint on negotiation (sec. 85). This is a special rule under which a bearer cheque always remains a bearer cheque.

(ii) With regard to "*order cheques*", the drawee banker is discharged by payment in due course of the cheque, which purports to be endorsed by or on behalf of the payee (sec. 85). Notice in this connection that the sec.

(a) *Joakimson v. Swiss Bank Corpn.* (1921), 3 K.B. 110.

(ai) *South Insurance Corp. v. National*

Provincial Bank (1936), 1 K.B. 328.

(b) *Wheeler v. Young* (1897), 13 T.L.R. 468.

protects a banker who pays an order cheque by a payment in due course, to the apparent indorsee thereof, although it turns out subsequently that the indorsement was forged and the indorsee had therefore no title to receive payment (c). The protection extends to cases where the endorsee's signature is forged (d). This is because, cheques (and banker's drafts) are a special exception to the general rule that a forged indorsement is, in law, no indorsement.

A banker is, however, not protected by a payment in due course, if the customer's (drawer's) signature is forged. The customer himself must not have been guilty of negligence, e.g. by leaving blanks in the body of the cheque (e). The customer is further bound in law to inform the banker immediately on becoming aware of the forgery. If he is guilty of unreasonable delay, he will be estopped from disputing the payment (f). Notice however that in order to relieve the banker from the consequences of paying money on a forged cheque, it is not enough for the banker to show that conduct of the customer, whether wilful or careless, enabled the fraud to be committed. He must show that the conduct of the customer in or immediately connected with the forgery or alteration, misled the banker into making the payment in question (g).

(iii) With regard to *cheques crossed generally*, the banker is discharged by paying the amount of the cheque to another banker, by a payment in due course (secs. 126 and 128).

(iv) Where a cheque is *crossed specially*, the banker is discharged, by paying the amount thereof to the banker specified or his agent for collection by a payment in due course (sec. 126).

(v) Where the cheque is crossed specially more than once, the drawee is bound to refuse payment thereof, unless the second banker is an agent for collection for the first (sec. 127).

Collecting Bank

When a Bank collects a cheque it may do so as a holder for value or as a mere agent of the holder, for the purpose of collection. In the latter case, the moneys are held by the collecting bank as trustee for the holder of the cheque (h). The question becomes important when the bank becomes bankrupt after the cheque is collected.

In the above case, I Bank handed over to N Bank 3 cheques drawn on the branch N Bank at T for collection. The T branch on receiving the cheques credited them to the head office and debited the amounts to the customers. N Bank thereafter went into liquidation. *Held*, N Bank in liquidation held the moneys as trustee for I Bank.

The position of a bank employed for collection was recently considered in detail by the Calcutta High Court and the following propositions were laid down :—

(1) A banker employed to collect or remit money is under a fiduciary obligation to account for and pay the money to his principal according to

(c) *Charles v. Blackwell* (1877), 2 C.P.D.

(d) *Jagjeeandas v. Nagar Central Bank*, 3 Bom. L.R. 226.

(e) *London Joint Stock Bank v. Macmillan & Arthur* (1918), A.C. 777.

(f) *Greenwood v. Martin's Bank* (1932), 1 K.B. 371.

(g) *Lewis Sanitary etc. Co. v. Barklay etc. Co.* (1906) 11 Com. C. 255.

(h) *Bank of India v. Off. Liquidator*, 53 Bom. L.R. 587.

directions. Ordinarily the agency does not terminate on collection but continues until payment.

(2) In the absence of instructions, the banker may remit the moneys to the principal by draft. The principal may accept the draft as conditional payment. If the draft is honoured and the money paid, the agency is terminated; if not, the ordinary obligation of the banker to pay the money is revived and the agency continues.

(3) The parties may agree that the banker may use the moneys collected for his own purpose under an obligation to the principal to repay an equivalent, instead of remitting the money to the principal in cash. In such a case, as soon as the banker uses the money for himself, a debt is created and the fiduciary obligation and agency terminate.

(4) During the continuance of the agency the money collected is held by the agent in a fiduciary capacity and in the event of the bankruptcy or winding up of the agent, may be followed and recovered, as long as it can be traced to a specific fund (i).

Negligence of Banker

The above rules refer to payment in due course by the banker. Payment in due course, means "payment in accordance with the apparent tenor of the instrument, in good faith and without negligence, to a person in possession thereof, under circumstances which do not afford reasonable ground for believing that the person claiming is not entitled to receive payment of the amount mentioned therein" (sec. 10).

The banker paying a cheque, therefore, is not protected, unless (i) he has acted in good faith, (ii) without negligence, and (iii) without reasonable ground to suspect the title of the holder. Thus payment after notice of drawer's insolvency, or after he has countermanded payment is not *bona fide* payment.

What is "negligence" depends on the facts of each case. Thus it is negligence to open an account for a customer without enquiring as to his identity and circumstances (j); it is negligence also, not to notice from time to time the customer's account and consider whether it is a proper or a suspicious account (k). Similarly, to pay a cheque which contains alterations, obliterations, or other kind of suspicious tampering therewith is negligence (l). To receive payment of cheque for a customer, when the cheque is drawn in favour of the customer's employer, without making inquiries, is also negligence (m). Similarly, a cheque payable to the customer in his official capacity if placed by the customer in his private account, requires inquiries (n). Payment of a cheque otherwise than in due course does not discharge the banker (sec. 129).

Protection to Banker

(i) A banker is protected if he pays an order cheque by a payment in due course, to a person who purports to claim under a valid indorsement (see ante).

(j) In *Re Calcutta National Bank*, 58 C.W.N. 783.

(j) *Ledbrooke & Co. v. Todd* (1914), 111 L.T. 43.

(k) *Lloyd's Bank v. Chartered Bank of India* (1929), 1 K.B. 46.

(l) *Slingsby v. District Bank* (1932), 1 K.B. 544.

(m) *Underwood Limited v. Bank of Liverpool, etc. Ltd.* (1924), 1 K.B. 775.

(n) *Ross v. London etc. Bank* (1919), 1 K.B. 678.

(ii) A banker is protected if he pays a bearer cheque to the bearer thereof, by a payment in due course, even though the cheque may be generally or specially endorsed (see ante).

(iii) A banker is protected if he pays a crossed cheque, on which the crossing is not reasonably apparent, as if it were uncrossed by a payment in due course.

(iv) A banker is not liable to the true owner if he receives payment of a cheque (crossed specially or generally) on behalf of a customer, if the customer's title to such cheque subsequently turns out to be defective (sec. 131). It makes no difference that he has credited the customer's account with the cheque before actually collecting the amount from the Bank (ibid). Notice however that the cheque must be crossed before it reaches the banker's hand. Further, failure to discover discrepancies in a cheque is not protected.

Refusal to pay cheque

If a banker without justification dishonours a customer's cheque, he is liable to compensate the customer for injury to his credit. Where overdraft facilities have been agreed to be given by a Bank to a customer, upto a fixed maximum limit, and the Bank holds sufficient securities of the customer to cover the maximum, a failure by the Bank to honour the customer's cheque within such limits is wrongful, even though the cheque may not have been accompanied by a specific demand for overdraft facility (n1).

A banker is justified in refusing to pay a customer's cheque in the following cases: (i) if the funds are not sufficient; (ii) if funds cannot be made applicable to the demand, e.g. if they are in fixed deposit account; (iii) if the banker has a general lien over the funds and subject to such lien, the banker has not sufficient funds; (iv) if the customer has countermanded payment of the cheque; (v) if a prohibitory order or garnishee order from the Court is served on the banker; (vi) if the customer dies; (vii) if the banker receives notice of the customer's insolvency or lunacy; (viii) if the account is closed; (ix) if the cheque is post-dated; (x) if the instrument is inchoate, ambiguous or not free from reasonable doubt; (xi) if the cheque contains material alterations, irregular signature or irregular indorsement; (xii) if the cheque is not presented within a reasonable time; (xiii) if it is not presented during usual business hours. Notice in this connection that entries in the pass book showing the amount standing to the credit of the customer are *prima facie* evidence against the banker of their correctness and a banker will be liable in damages if he dishonours a cheque drawn by the customer in favour of a third person on the faith of such entries (o).

Where a cheque is dishonoured, notice of dishonour must be given to the indorser in order to make him liable. If no such notice is given, indorser will be discharged (p).

"Account payee"

These words on a crossed cheque are in law regarded as a direction to the banker collecting payment of the cheque that the proceeds of the cheque

(n1) *Brahma Samsherjung v. Chartered Bank of India, A.I.R. (1956) Cal. 399.*
(o) *Holland v. Manchester Banking Co.*

(1909), 25 T.L.R. 386.

(p) *Mahomad v. Merjaffar, A.I.R. (1936) Lah. 796.*

are to be credited to the account of the payee. The collecting banker therefore is guilty of negligence if after collecting the amount he credits it to any other account, without making proper inquiries as to the title of such other person (q). These words however do not, in law, affect the liability of the paying banker. A cheque crossed generally or specially with the words "account payee", does not impose a liability on the paying banker to see that the amount paid by him is applied by the other banker to the payee's account. His obligation ceases when he has paid the amount to the other banker, under the crossing (r). Similarly, the banker who collects such a cheque for another banker is also not obliged to see that the banker for whom he collects such a cheque, pays the amount thereof to the payee's account (s). Notice that a cheque crossed "account payee" is still negotiable (t) though a bill of exchange payable to payee only is not negotiable (u).

Drafts

These are bills of exchange issued by a banker on his branch office. They resemble cheques and by sec. 131A the same rules are made applicable to these drafts, as are applicable to cheques, so far as forgery, crossing and collecting of such drafts by bankers are concerned (see ante).

Bank's drafts are bills drawn by one banker on another in favour of a third party or by a branch of a bank on another branch of the bank or on the head office of the bank. Notice that sec. 131A refers only the second class of banker's drafts, which are by that sec. placed on the same footing as cheques. Banker's drafts of the first kind are therefore not equivalent to cheques. In England they are not regarded as negotiable instruments (v).

PROMISSORY NOTES

Definition: A "promissory note" is defined by sec. 4 as "an instrument (i) in writing (not being a bank note or currency note) (ii) containing an unconditional (iii) undertaking (iv) signed by the maker (v) to pay a certain sum of money only, (vi) to or to the order of a certain person or to the bearer of the instrument".

A promissory note, in order to be so, must fulfil all the above conditions. It must be in writing. No particular form however is necessary. It may take the form of a letter even. It must be signed by the maker. "Signature" includes pencil, lithograph and also printed signature. The intention to sign, however, must in all cases be proved (w). The promissory note must contain an undertaking or *promise to pay*. This is the foremost distinguishing feature of a promissory note. Thus a mere acknowledgment of liability for a debt is not enough nor also an admission of a debt, with an undertaking to pay interest thereon (x). A request for a loan, with an assurance that it will be repaid, is also not a promissory note (y). If it does contain a promise to pay, however, the fact that other

(q) *House Property Co. v. London etc. Bank* (1915), 84 L.J. K.B. 1846.

(r) *Akrokerrri, etc. Ltd. v. Economic Bank* (1904), 2 K.B. 464.

(s) *Importer's Bank Ltd. v. Westminster Bank* (1927), 2 K.B. 297.

(t) *National Bank v. Silke* (1891), 1 Q.B. 435.

(u) *Hiberian Bank v. Gysin* (1930), 1 K.B. 483.

(v) *Capital & Counties Bank v. Gordon* (1903), A.C. 240.

(w) *Laxmibai v. Ganesh*, 25 Bom. 373.

(x) *Bharata v. Vasudevan*, 37 Mad. 1.

(y) *Tirupathi v. Rama Reddi*, 21 Mad. 49.

terms besides the same are contained in the instrument will not make it less a promissory note. Thus a statement that title deeds have been deposited as security for repayment, will not affect the promissory note (z).

The Privy Council has recently held in *Akbarkhan v. Attarsing*, 17 Lah. 557, that the question whether a document is a promissory note, is one of construction *depending upon the intention of the parties* as appearing from the terms of the document. The purpose for which the document has come into existence is therefore the test and it is only documents which have come into existence for the purpose of recording an agreement to pay money and nothing more (though they may, of course, state the consideration), that are now to be regarded as promissory notes under sec. 4. Thus receipts for payment of money (though containing assurance of repayment), and agreement for payment of money are not pro. notes. Similarly, a statement of account showing the balance due and stating that the amount was "to be paid up in full in the next month" is not a pro. note (*ibid*).

The promise, further, must be unconditional. Thus a promise to pay a sum of money, a certain number of days "after A's marriage", is not a pro. note (see *ill.*). The sum must also be certain. A promise to pay "Rs. 500 and all other sums that may be due" is not a good pro. note. The sum may be payable by instalments. The medium of payment must be money only, a promise to repay "Rs. 500 and to deliver a horse on a certain day" not being a pro. note (see *ill.*).

The payee also must be certain. A pro. note not mentioning the name of the payee is not a good note. The intended payee, however, can, in such a case, fill in the blank. Notice that a pro. note payable to the maker or his order, is an inchoate instrument, which becomes effective in law only when the maker indorses it in favour of another. A note in favour of a fictitious person is treated as payable to bearer. A note can be made in favour of a community (a), though not in favour of an uncertain body of persons, e.g. in favour of partners of a firm "for the time being". Alternative payees are permissible in law.

Calling a document a promissory note will not make it so. It must fulfil all the requirements of secs. 4 and 13. One of such requirements is that the promisor and promisee (payee) must both be certain. Thus where the words of a writing were "we as well as our successors are bound hereunder to fulfil your dues whenever and wherever you or your successors demand the sum", *held*, the document was not a promissory note (b).

Notice that the place of execution, the date of execution and the time of payment of a pro. note are not essential elements of a pro. note. When no time is mentioned, the note is payable on demand (sec. 19).

A "bank note", i.e. a note issued by a banker, payable to bearer on demand and a "currency note", i.e. a note issued by Government, payable to bearer on demand, are not included in the definition. The former is in fact illegal under the Reserve Bank Act (see *ante*).

"Government promissory notes" are within the definition. These are promissory notes issued by Government for loans raised by the Government.

(z) *Ramachandra v. Shesha*, 17 Mad. 85.

(a) *Budaveram v. Noota*, 44 Mad. L.J.

(b) *Ambalal v. Jawarlal*, A.I.R. (1953) Cal. 758.

They are negotiable instruments capable of being transferred by indorsements. The rights of the indorsee however and the method of their renewal are governed by the Indian Securities Act, 1920, and by Public Debt (Central Government) Act (18 of 1944). Under the last Act it has been held that if a Government promissory note which has a forged endorsement on it is converted or renewed by Government, the true owner of the old promissory note has no right against the Government or the Reserve Bank of India for the price of the note. Under sec. 19 of the last Act, the only remedy of the true owner is against the person who has a title to the security as a result of the renewal by the bank (c).

Notice that the definition of a pro. note given above is exhaustive ; what does not fall within the terms thereof, is not a promissory note. Debentures of the Bombay Municipality and the Bombay Port Trust have been held to be pro. notes (d).

In a suit based on a promissory note, it is not permissible for the person signing the document to lead evidence to show that he signed as agent for a person whose name does not appear on the document (e).

Promissory notes : their nature

A pro. note is akin to a bill of exchange, except for this difference that whereas in a bill of exchange, there are three interests concerned, viz. that of the drawer, the acceptor and the payee, in a promissory note, there are only two interests concerned, viz. that of the maker and the payee. The drawer of a bill differs from the maker of a pro. note, because while the liability of the former, in case of an accepted bill, is only secondary, the liability of a maker of a pro. note is, from its inception, primary. The maker of a pro. note, in fact, occupies the position of an acceptor of a bill of exchange. This is the reason why the whole law as regards presentation, acceptance, dishonour, and protest with regard to bills of exchange is absent in case of pro. notes. Barring this fundamental difference, and a few others to be presently noticed, the law of bills of exchange applies generally to pro. notes also.

Four kinds of pro. notes are recognised by the Act : (i) a note payable to A or order, (ii) a note payable to A, without words restricting transfer ; (iii) a note payable to the order of A and (iv) a note payable to bearer. All these types of notes are nego. insts. A note payable to A only, however, is not negotiable, though a note payable to "Dhani" is regarded as valid (f). By Ordinance 17 of 1946 of the Central Government, no bank can now make or issue any pro. note expressed to be payable to the bearer of the instrument. Penalty for the contravention of the order is a fine amounting to twice the amount of the note.

A pro. note may be a foreign or inland instrument. A pro. note may be payable "on demand", or "at sight", or "after sight" (sec. 21). The rules as regards "maturity" and days of grace apply to pro. notes also (sec. 22). The rules as regards a holder in due course also apply in case of pro. notes.

(c) *Mascarnhas v. Mercantile Bank of India*, 34 Bom. L.R. 1; *Vasudeo v. National Savings Bank*, 54 Bom. L.R. 765.

(d) *Mascarnhas v. Mercantile Bank of India* (supra).

(e) *Pramod Kumar v. Damodar*, A.I.R. (1953) Orissa 179.

(f) *Jetha Parkha v. Ramchandra*, 16 Bom. 689.

As regards payment, in absence of a contract to the contrary, the maker of a note undertakes to pay the amount thereof at maturity, according to the apparent tenor of the instrument (sec. 32), his liability being primary (sec. 37). As between subsequent indorsers and the maker, the former are liable only as sureties for the maker, each one of the indorsers *inter se* being liable as a principal debtor to each subsequent indorser (secs. 37-8). The rules as regards consideration and the consequences of its failure also apply in case of pro. notes (secs. 43-44).

A bearer pro. note can be negotiated by delivery only while an order pro. note can be negotiated by endorsement and delivery (sec. 46). A pro. note may be delivered as an "escrow" (sec. 47).

Presentment in case of promissory notes

Generally speaking, no presentment to the maker is necessary in case of a pro. note payable "on demand", because it is the duty of the debtor to find out his creditor, within the realm and to pay him his due (sec. 64). Presentment to the maker however is necessary in the following cases :

(i) Where the pro. note is payable a certain period "after sight", in such a case if the note is not presented to the maker, within a reasonable time after it is made, and in usual business hours on a business day, by a person entitled to demand payment thereof, all parties thereto (i.e. the maker and the indorsers) are discharged from liability (sec. 66).

(ii) A pro. note (whatever its nature), must be presented to the maker for payment by the holder thereof, in order to make the other parties (i.e. the endorsers) liable on the note (sec. 64).

(iii) A pro. note payable a specified period "after date" or "after sight", must be presented to the maker at maturity (sec. 66). If the note is payable by instalments, it must be presented on the third day after the date fixed for payment of each instalment (sec. 67).

(iv) If the note is made payable at a fixed place and not elsewhere, no party (including the maker) will be liable thereon unless it is presented to the maker at that place (sec. 68).

(v) If the note is made payable at a fixed place, the maker will not be liable unless it is presented at that place (sec. 69).

(vi) A pro. note payable on demand, must be presented for payment within a reasonable time after it is received by the holder (sec. 74). Delay in presentment due to unavoidable causes may be condoned (sec. 75A).

The rules as regards discharge of liability on a pro. note are generally the same as in case of bills of exchange. Notice that the maker of a pro. note is estopped from denying the validity of the note, as against a holder in due course (sec. 120). Similarly, he is estopped from denying the payee's capacity to indorse the note, as against a holder in due course (sec. 121). An indorsee of a note is also estopped from denying the signature or the capacity to contract of any prior party thereto (sec. 122).

HUNDIS

These are bills of exchange in the vernacular language, which have been in common use in our country for purposes of business from at least the 10th century A.D. and which have been recognised by law as valid and effective negotiable instruments. The rules with regard to "hundis" are

determined by custom. A "hundi" when discharged is called a "khokha". Technical rules laid down by the Nego. Ins. Act as regards presentment, etc., do not apply to Hundis, which, in such technical matters, are governed by the custom or usage of merchants of the place where the Hundis are drawn. The necessity of a notice of dishonour to a prior endorser, in order to make him liable on the Hundi, is not a mere technical matter but a matter of principle. If such notice is not given within a reasonable time, the prior endorsee would be discharged from liability and this would be so, even if the Act is not applicable to the place where such Hundi is drawn (f1). A hundi may be either (i) a "darshani" hundi, i.e. one payable at sight or (ii) "muddati", i.e. one payable after a certain time. Notice that where a hundi is drawn by way of renewal of and in substitution of a previously accepted hundi, the substitution is conditional on the substituted hundi being accepted by the drawee. Where it is not so accepted and the condition therefore is not fulfilled, the original accepted hundi remains in full force against the acceptor and he is liable to be sued on it (g). The various kinds of hundis known to our trade are as follows:—

"Dhani Jog hundi": This is a hundi payable to "dhani", i.e. owner. It is payable to any owner, holder or bearer. It is a negotiable instrument payable to bearer (h).

"Nam Jog hundi": This is a hundi payable to a named party or his order. Generally it contains a description of the person mentioned; when this is so, it is not transferable. In absence of it, however, it can be negotiated by indorsement.

"Shah Jog hundi": This is a hundi payable only to a 'Shah', i.e. a respectable person or a person of recognised credit in the market (i). Such a hundi is not payable to bearer, but only to a "respectable bearer" and that only when there is a proper indorsement in favour of the "Shah" by the last indorser, who presents it for payment (j). According to the Bombay High Court (k) a "Shah Jog hundi" at its inception, is a hundi which passes from hand to hand by delivery, without any indorsement being necessary. When, however, it reaches a "Shah" who presents it for payment, its negotiability ceases. If, thereafter, the "Shah" endorses it in favour of a man of straw, the drawee is within his rights in refusing to pay the amount to such person. This is because the drawee is entitled to have the immediate responsibility of the "Shah" established as between himself and the "Shah". Where a "Shah Jog hundi" bears a special indorsement, it ceases to be a bearer hundi and any person taking it after such indorsement should comply with the requisitions as they appear on the face of the hundi and examine the title of the holder in the light of the indorsement (ibid). When a "Shah Jog hundi" is presented to the drawee, the latter is bound to make proper inquiries as to whether the person presenting is in fact a "Shah" and whether the indorsement in his favour is genuine. A payment of such a hundi by the drawee without such inquiries will make him liable to the drawer in damages (l). If in spite of such inquiries, it turns out subsequently that the 'Shah' who was paid had no title to receive the payment,

(f1) *Kanhyalal v. Ramkumar*, A.I.R. (1956) Raj. 129.

(g) *Motilal v. Unao Commercial Bank*, 32 Bom. L.R. 1571 (P.C.).

(h) *Jetha Parkha v. Ramchandra*, supra.

(i) *Bansidhar v. Jwala Prasad*, 16 Bom. L.R. 434.

(j) *Murlidhar v. Hukamchand* (1932), Lah. 312.

(k) *Champaklal v. Keshrichand*, 28 Bom. L.R. 897.

(l) *Ramprasad v. Shrinivas* (1925), Bom. 527.

e.g. if the indorsement in his favour was forged, the 'Shah', according to a well-known custom of merchants, is bound to return the amount paid, to the drawee, with interest at 6 per cent unless, he (i) either produces the drawer or (ii) the person who committed the forgery (m). The drawee, however, on his part, must give notice to the 'Shah' of the forgery, as soon as he discovers it. Undue delay will disentitle the drawee from claiming reimbursement (n).

Notice that a drawee of a Shah Jog hundi is not discharged from liability to the true owner, by reason of his paying the amount to the Shah (o). An indorsee from the payee of a Shah Jog hundi is presumed to be a holder in due course, till the contrary is proved (p).

A Shah Jog hundi differs from an ordinary bill of exchange in that (i) in case of such a hundi, its acceptance is not written across the face of it, but particulars thereof are entered into the books of account of the drawee and (ii) such a hundi is not generally presented for acceptance before or after it is due but only for payment. A notice of dishonour however is necessary in order to make the drawer of the hundi liable thereon (q). Indeed, such notice is necessary in cases of all hundis, unless a custom to the contrary is established (r).

Notice that a "Shah Jog hundi" is not a negotiable instrument because it is not payable to order or bearer but to a Shah. When such a hundi is the subject of a conversion, therefore, the true owner can sue the drawee for the same and there is no custom which absolves the latter from liability on the ground that the hundi is paid to a Shah (s).

"Jokhmi hundi": This is a hundi drawn against goods, shipped on a named vessel. It resembles a policy of marine insurance. The drawer of the hundi is the consignor who draws for the value of the goods on the consignee. The drawer then gets the hundi discounted by a broker, to whom he hands over the proper shipping documents, the broker charging a particular commission, for his services (which resembles a premium). The broker, then, will present the hundi and the documents to the consignee, who is bound to pay the amount to the broker, if the vessel has arrived safely in port. If the ship is lost, the broker bears the whole loss (i.e. the risk).

"Jawabi hundi": This is a hundi employed to send money to distant places and resembles a money order. The drawer (remitter), writes to the payee and delivers the letter along with the remittance to a banker. The latter sends the letter to his correspondent at the named place with instructions to pay the amount to the payee. On payment, the payee signs his receipt on the letter, which is then returned to the remitter, in the same way.

"Zikri Chit": This is a hundi in frequent use amongst marwadi shroffs. It consists of a letter given by some prior party to the holder, and addressed to a person at the place where the bill is payable requiring such person to pay the amount of the hundi, in case the drawee fails to pay the same. It creates something like an "acceptor for honour" and it is valid in law, though the provisions of the Act with regard to "acceptor for honour" are not complied with.

(m) *Davalatram v. Bulakhidas*, 6 Bom. H.C.R. 24.

(n) *Bansidhar v. Jwalaprasad*, *supra*.

(o) *Madhavdas v. Devidas*, 59 Bom. 97.

(p) *Sakharam v. Gulabchand*, 16 Bom.

L.R. 743.

(q) *Motilal v. Motilal*, 6 All. 78.

(r) *Krishnaji v. Hari Valji*, 20 Bom. 48.

(s) *Jessarani v. Virbhandas*, A.I.R. (1947), Sindh 40.

CHAPTER XIII

AFFREIGHTMENT

Contract of affreightment: This means a contract of carriage of goods by land or sea for a price. The term is generally applied to contract for carriage by sea. A contract of affreightment may take the form of (i) a "charter party" or (ii) "a bill of lading".

Charter party: This is defined as "an agreement by which a shipowner agrees to place an entire ship or a part of it, at the disposal of a merchant, for the conveyance of goods, binding the shipowner to transport them to a particular place, for a sum of money which the merchant undertakes to pay for the carriage". The person whose goods are so carried is called the "charterer". The price paid or agreed to be paid by the merchant to the shipowner for such carriage is called "freight".

Bill of Lading: A "bill of lading" is defined as "a document acknowledging the shipment of goods, signed by or on behalf of the carrier, and containing the terms and conditions upon which it has been agreed that the goods are to be carried". It is also described as "a contract for the conveyance of goods in a general ship".

Difference between the two: The two documents, however, differ from each other in several material respects: (i) A "bill of lading" is an acknowledgment of the receipt of goods on board the ship; a charter party is not; (ii) a bill of lading is a "document of title to goods", as defined by the Sale of Goods Act; a charter party is not such a document; (iii) a charter party may amount to a demise, i.e. a lease of the ship or a part thereof; a bill of lading conveys no such implication; (iv) both documents, however, resemble each other, in that they both contain the terms and conditions of the particular contract of affreightment.

Their relation inter se: Sometimes both the above documents co-exist, e.g. where the charterers want to carry goods of other parties also on board the same ship or where the charterers, having loaded the ship with their own cargo, want to deal with parts of the cargo, while the goods are still in transit. The rule of law laid down in such cases is that (i) as between the shipowner and the charterer, the charter party is the governing document, the bill of lading merely operating as an acknowledgment of the receipt of goods; (ii) as regards assignee of the bill of lading and the shipowner, the bill of lading is considered to be the governing document, unless by reference, the terms of the charter party are treated as incorporated therein, e.g. where the bill of lading provides "freight and all other conditions as per charter party" (t). Notice however that, even where this is so, only those terms of the charter party are incorporated in the bill of lading as concern the consignees. Thus a term in the charter party that "goods carried on deck are at the merchants' risk", was held not incorporated in a bill of lading, by reason of such reference, as such a term refers to the consignors and not to the consignee (u).

A charter party need not be under seal. It is required to be stamped in India with a one rupee stamp (Art. 20, Stamp Act). A bill of lading requires a 4 anna stamp (Art. 14, Stamp Act). Notice that where a charter party creates a demise of the ship or part thereof, the ship goes out of the control of the shipowner and the master and the crew become the agents of the charterers. Generally, however, under a charter party, the shipowner retains ownership of the ship, the charterer acquiring the right to place his goods on board and have them carried by the ship to the port of discharge. It is a question of construction whether a charter party falls under the first or second class.

CHARTER PARTY

Kinds of charter parties: A charter party may be: (i) a "voyage charter party", i.e. extending to a particular voyage or voyages or (ii) a "time charter party", i.e. extending over a definite period of time, irrespective of the number of voyages performed.

(t) *Oriental Steamship Co. v. Taylor* (1893), 2 Q.B. 521.

(u) *Serraino v. Campbell* (1891), 1 Q.B. 283.

Terms of charter party

These are of two kinds: (i) implied terms, i.e. those terms which law implies in all charter parties, unless they are specifically excluded and (ii) express terms, i.e. terms which the parties have expressly agreed to and embodied in the charter party. A charter party generally is drawn up in a special form commonly used in the trade, with such additions and alterations as the circumstances of each may require. A common form of a charter party is given below.

Notice that some terms of a charter party are given by law a special significance. They are therefore called "*conditions*", the breach whereof would avoid the whole contract. Such terms are, the name of the ship, the nationality of the ship, the class to which the ship belongs and a few others. Other terms are regarded by law as ordinary terms, the breach of which only entitles the party suffering thereby to damages, e.g. tonnage, seaworthiness, etc. Whether a term amounts to a "*condition*" or not, is a question of construction.

Implied terms: In all contracts of carriage by sea, the following terms are implied:

(i) that the ship is "seaworthy". "Seaworthiness" means that the ship is reasonably fit to encounter the ordinary perils of the sea, in view of the adventure in question. This is called an implied "*warranty of seaworthiness*". It is an assurance given by the shipowner, at the time of entering into the charter party, that (a) the ship is fit to encounter the ordinary perils of navigation and (b) to carry the particular cargo. It includes the following: that the ship is properly constructed, that its machinery is in proper working order, that it has efficient crew and master, that it is sufficiently provided with the necessities of the voyage, e.g. coal, oil, etc.; that it is not overloaded or badly loaded. Bad stowage will amount to "unseaworthiness", if it endangers the safety of the ship, though not, if it only endangers the cargo. Notice that the "*warranty of seaworthiness*" attaches only at the time of sailing. Once the vessel has sailed or the goods loaded, the warranty does not operate. If the voyage, however, is, by the contract, divided into stages, the warranty must hold good at the beginning of each stage. At common law, the warranty was absolute. Under the Carriage of Goods by Sea Act, 1924, however, it is not absolute now but only that the shipowner shall use due diligence to make the ship seaworthy. If the cargo owner discovers the unseaworthiness before the commencement of the voyage, he can repudiate the contract unless the defects can be repaired within a reasonable time. After the voyage has started, however, he can only recover damages for loss caused by its breach.

(ii) Another implied term is that the ship shall be ready to commence the voyage and shall carry out the same with all *reasonable dispatch or diligence*. A breach of this term entitles the charterer to repudiate the contract, if the delay is such as goes to the root of the contract and makes the marine adventure different from what it was originally intended to be. If it is not so, the only remedy is damages.

(iii) That the ship shall carry out the voyage in the usual and customary manner, and *without deviation*.

Deviation: "Deviation" means the going off from the usual or customary course of voyage between two given termini. The shipowner is bound to carry out the voyage by the usual or the customary route. If such a course is deviated from: (a) the whole contract of affreightment becomes void, from the beginning of the voyage, no matter where and when the deviation took place. (b) Further, the "excepted risk clause" (see below) will not avail the shipowner. Thus where the "excepted risk clause" in a charter party exonerated the shipowners from liability for loss caused by enemy action, and the ship having "deviated", was torpedoed by an enemy submarine, after the deviation had ceased, it was held that the shipowner was liable for the loss caused. "Deviation" however is allowed where it is necessary to save life or to secure the safety of the ship. This is so, even though the danger is caused by "unseaworthiness" (v). In case of bills of lading governed by the Carriage of Goods by Sea Act, 1924, deviation is now allowed to save property also. Charter parties and bills of lading generally contain a deviation clause, e.g. giving liberty to call at certain ports. Such

(v) *Joseph Thorley v. Orchis S.S. Co.* (1907), 1 K.B. 660.

clause is to be construed in relation to the commercial object of the voyage. It does not give a general right to deviate from the usual or the customary route.

(iv) Another implied term in all contracts of affreightment is one binding the shipper not to ship *dangerous goods*. Such goods must not be consigned on board a ship unless their nature is clearly marked on the outside of each package and written notice of the same is given to the master or the shipowner.

Form of charter party: The following is a usual form of a charter party:

It is this day mutually agreed between Messrs. (A.B.), agents for owners of the good ship or vessel called (The James Scott), A1 and newly coppered of, etc. of the burden of 340 tons register measurement or thereabouts, whereof (C.D.) is master *Now at* (Malta) and Messrs. (E.F. of Liverpool) merchants, that the said ship, being tight, *staunch and strong and every way fitted for the voyage*, shall, with all convenient speed proceed to London, and *there load* in the usual and customary manner, a *full and complete cargo*, of lawful merchandise (say about 400 tons in weight) and therewith proceed to (Hong Kong or Shanghai) as ordered before sailing or as *near thereunto as she may safely get*, and *there deliver the same in the usual manner*, agreeably to bills of lading; after which she shall load there or if required proceed to one other safe port (in China) and there load *always afloat* in the usual and customary manner from the agents of the said charterers, a full and complete cargo of tea or other lawful merchandise not exceeding what she can reasonably stow and carry over and above her tackle, apparel, provisions and furniture, the cargoes being brought to and taken from alongside the vessel at the charterer's risk and expense, which the said merchants bind themselves to ship and being so loaded shall therewith proceed to (Liverpool or London) as ordered on signing bills of lading, abroad, or so near thereto as she may safely get and there deliver the same in the usual and customary manner to the said charterers or their assigns, they paying *freight* for the same at the rate of (£7 10s. per ton of 50 cubic feet) for tea delivered, for the round out and home, a deduction of (5s. per ton) to be made if ship be discharged and loaded at (Hong Kong), other goods, if shipped, to pay in customary proportion; in consideration whereof the outward cargo to be carried freight free, payment whereof to become due and be made as follows:—(then follow terms). Ship is to have liberty to put on board 80 tons of () or other dead weights and to retain it on board during the voyage. *Thirty running days* (Sundays and holidays excepted) are to be allowed the said merchant if the ship is not sooner dispatched for loading in (London) and forty-five like days for all purposes abroad, and ten days *on demurrage* over and above the said *lay days* and the time herein stated, at (£10 sterling per day) paying day by day as the same shall become due. The time occupied in changing ports not to count as lay days. *Charterer's liability under this charter party to cease* on the cargo being loaded, the master and owners having a *lien on cargo* for freight and demurrage. The master to sign bills of lading at such rates of freight as may be required by the agents of the charterers, without prejudice to this charter-party.

The Act of God, the King's enemies, restraint of princes and rulers, fire and all and every other damages and accidents of the seas, rivers and navigation of what nature and kind soever, throughout the voyage, *being excepted*.

The vessel to be consigned to charterer's agent abroad free of commission. On the return of the ship to (Liverpool) she shall be addressed to (G. H. and Co.) brokers or to their agents, at any other port of discharge. Penalty for non-performance of this agreement, the estimated amount of freight.

Clauses of charter party

"Name": The name of the ship which is to carry out the voyage is a "condition" of the charter party. If a ship of another name is substituted in its place, the charterer is entitled to avoid the contract. *Nationality* of the ship as described in the charter party is also another important term of the contract. If the ship's nationality is different or is changed during the course of the voyage, the charterer is entitled to treat the whole contract as broken. **"Class":** The description of the ship as belonging to a particular class, e.g. A or B, or B₁ or C class, conveys to the charterer the then condition and standing of the ship: ships being classified according to their existing condition by

the Admiralty. If the ship turns out to be of a different class, a "condition" of the contract is broken, and the charterer is not bound by the contract. "Now at": The place where the ship actually is at the time the charter party is entered into is mentioned here. This is important because it indicates to the charterers, when the ship will probably arrive at the port of dispatch and so prepare to load the cargo accordingly. If the statement is untrue, the charterer is entitled to avoid the whole contract because this term is a "condition" of the charter party (w).

"Tight, staunch and strong and every way fitted for the voyage": This amounts to an express "warranty of seaworthiness" for which see ante.

"Shall there load": It is the duty of the shipowner to bring the ship at the usual or agreed place of loading and give notice to the charterer of the ship being ready for loading. Thereafter the charterers must produce the cargo, bring it "alongside" the ship and deliver it to the servants of the shipowner. The shipowner is then responsible for proper stowage of the cargo. The charterer is liable, if he fails to produce the cargo, though the failure is not due to any fault of his own. "Alongside" means "to and from the ship's tackle in such position that the persons concerned can begin to act on the goods."

"Loading" is a joint act of the shipper or charterer and the shipowner. Each has to do his part and help the other reasonably to do his part. The shipper must bring the goods alongside the ship and lift them up to the rail of the ship. The shipowner must then be ready to take such cargo on board and stow it properly. The shipper must bring the cargo alongside within sufficient time to enable the shipowner to stow it properly (x).

"Full and complete cargo": This means as much cargo as the ship can hold. This is so, even if, in other clauses, the carrying capacity of the ship has been differently described. Where such words are used, the charterer is bound in law to load cargo to the full capacity of the ship, though the carrying capacity actually mentioned may be more or less. The result is the same, if only the word "cargo" is used. Where however the words are "a full and complete cargo say about 1,100 tons", the charterer is not bound to ship cargo to the full capacity of the ship but only up to 1,100 tons and 3 p.c. more, though the ship's capacity may be 1,600 tons (y). The above words do not oblige or authorise the charterer to load deck cargo.

Lawful Merchandise: In order to be "lawful merchandise", the goods loaded under a charter party must not only be such as could be loaded without breach of the law at the port of loading but must also be such as could be lawfully carried and discharged at the port of discharge (z).

"So near thereat as she may safely get": The shipowner is bound to take the ship to the port of dispatch or destination and bring it there at such place, as is usual for ships of that kind to load or unload. The consignor is not bound to load and the consignee is not bound to unload till this has been done and they have notice of it. It may sometimes happen however that owing to war, blockade, strikes, lockout or damage to ship, it is not possible to bring the ship at such place. The words of the above clause protect the owner in such eventuality.

"Deliver the same in the usual manner": The shipowner is bound to bring the ship to the named place with reasonable dispatch and when there, with reasonable dispatch, to discharge (a). The shipowner is bound to place the cargo on the rail of the ship and in such a position that the consignee can take delivery of it. The consignee or the charterer is bound to provide appliances for taking delivery, which must always be taken in the agreed period.

(w) *Bentsen v. Taylor & Sons* (1893), 2 Q.B. 274.

(x) *Harris v. Best Relay Co.*, 9 T.L.R. 149.

(v) *Morris v. Levison* (1876), 1 C.P.D. 155.

(z) *Laolge Campania v. John Glynn & Son Ltd.* (1953), 2 All E.R. 327.

(a) *Nelson v. Dahl* (1897), 12 Ch.D. 592.

"Always afloat": Under this clause, the shipowner is bound to send the ship to a port, in which she can safely be, with full cargo, without grounding. If, with the knowledge of the shipowner, the ship is sent to a port, where owing to the state of the tides, it is not always afloat, the charterer would not be liable for the delay.

Freight

This is the consideration paid or agreed to be paid by the charterer for carriage of goods by sea in a ship belonging to the shipowner. It is generally calculated in tons of fixed cubic feet measurement (see form). When heavy goods are being carried, e.g. iron ore, the calculation is by weight. Generally freight is not payable till the termination of the entire voyage. No freight is payable if the marine adventure represented by the charter party is only partly performed. Thus if the shipowner abandons the ship under stress of weather, before the agreed voyage is completed, and the cargo owners are subsequently able to recover the cargo by salvage, they are entitled to retain the same without any liability for freight; similarly, also, if goods are not delivered by reason of any of the excepted perils.

Various kinds of freights are known: (i) **"Advance freight"**: This is freight payable by agreement in advance of or before the commencement of the voyage. Failure to complete the voyage will not entitle the cargo owner to a refund of such freight. It is payable at the moment of starting, though if not so paid, and the ship is lost on the voyage, such freight is still recoverable by the shipowner. If the goods, however, are destroyed before starting, such freight cannot be recovered.

(ii) **"Dead freight"**: This is freight payable by the charterer as damages for failure to produce or load the agreed amount of cargo.

(iii) **"Lump sum freight"**: This is one entire sum to be paid for the hire of the ship for an entire service. The shipowner is entitled to the whole sum if he delivers any part of the cargo. If the whole cargo is lost, no freight is payable but if a substantial portion is delivered and the residue is lost by any of the "excepted perils", the whole amount is recoverable though the ship does not arrive.

(iv) **"Freight pro-rata"**: If part of the original contract of charter party is performed by the shipowner, and if at a point short of destination, the goods are accepted by the charterer or his agents in such a manner, that further carriage is dispensed with, a contract to pay proportionate compensation for the benefit actually received, i.e. for the voyage actually performed, arises, which is called "freight pro-rata" (b).

Shipowner's lien: At Common Law, a shipowner has a lien on cargo for freight and demurrage due to him for its carriage. It extends to all property consigned on the same voyage under the same contract by the same person. Delivery of part of the goods does not destroy the lien on the rest. It is a possessory lien which is lost on the cargo being delivered. It extends to cover general average contributions and expenses incurred in protecting the goods. There is no lien for "dead freight", however, unless there is a custom or agreement to the contrary.

Under the Merchant Shipping Act, 1894, the shipowner is now entitled to discharge the cargo from the ship into a bonded warehouse with a written notice to the custodian of his lien. In such a case, the lien is not lost by parting with the possession of the goods. The shipowner can, under the Act, also sell the goods by public auction after a fixed period of time.

Loading and unloading time: This is time fixed and allowed by the charter party to the charterer and his agent for the purpose of loading and unloading the ship. The time begins to run when notice is given to the charterer or his agents of the arrival of the ship at the agreed port and of its readiness to load or unload. It is generally fixed as so many tons per running day. If more than the agreed time is taken, the charterer, has to pay "demurrage". If less time is taken, the shipowner pays the charterer, what is called "dispatch money". Notice that a statement in a charter party that the ship

shall be ready to load at a certain day or that she is at a certain place at the time when the charter party is entered into is regarded as a "condition" of the charter party. If it is untrue, the charterer will be entitled to rescind the contract.

Lay days: These are days allowed by the charter party for loading and unloading. They begin to run when the ship arrives at the place agreed upon and the charterer has notice of its readiness to load or unload, each day being counted from midnight to midnight. If Sundays and holidays are desired to be excluded, this must be specially provided for; so also, the time taken up in shifting from one port to another for purposes of loading or unloading. If lay days expire without loading or unloading being completed, "demurrage" becomes payable. If lay days expire, every part of a day, which is over the agreed time, counts as a whole day. Where the agreement is to load at tons "per weather working day", overtime, which is less than $\frac{1}{2}$ day, and is caused by bad weather, will count as $\frac{1}{2}$ day only (c). "Working Day" is calculated by the number of hours customarily worked per day in a port and not a day of 24 hours. "Weather working day" means the period of "working day" computed as above, from which the number of hours during which work is suspended owing to weather is deducted (c1).

Demurrage: This is "agreed additional payment, for an allowed detention of the ship, whilst loading or unloading, beyond the period specified in the charter party". It also means compensation, by means of unliquidated damages, for undue detention of the ship, not specifically provided for in the charter party (d). Such additional payment is generally calculated "per day" (see "lay days" ante). The charterer is bound in law to pay demurrage so long as the ship is in such a condition, that she cannot be handed back to the use of the shipowner though the situation has not arisen through any fault of the charterer. If however the delay is due to the default of the shipowner, the charterer is not liable for demurrage. Demurrage is payable for extra detention of ship after it has "arrived" at the place or port of destination. It may be a question as to when a ship can be called an "arrived ship". The answer depends on the words used in the charter party (e). Time taken up by ship in waiting for a berth, may be included in "loading time", if so provided by the terms of the chartered party (e1).

"Charterer's liability to cease": This is called the "cesser clause". It means that the charterer shall be free from all future liability after the stage mentioned in the cl. is reached, generally after goods are loaded. This cl. is generally interpreted as complementary to the lien cl. (see ante) so that no liability which is imposed by law on the charterer, will be destroyed thereby unless it is recreated in someone else, by the lien cl. It is a question of construction whether the cl. releases the charterer from prior liability.

"Excepted perils clause": This cl. comprises various classes of risks, for which the shipowner *does not take responsibility*, if any damage results thereby. The shipowner is, by this cl., exonerated from liability, for loss occasioned by any of the causes enumerated in this cl. (f). These are precisely the risks, which a marine insurance policy is designed to protect against. Thus a charter party and a marine insurance policy are supplementary of each other. The cl. generally mentions all kinds of possible risks of a sea voyage. Some of them are explained below (see also "Marine Insurance" seq.). Notice that the shipowner can take advantage of the "excepted risk cl." only if (i) the loss is not caused by the negligence of his servants or (ii) by breach of the implied warranty of seaworthiness.

Act of God: This means "any accident causing damage to goods, which is due to natural causes, without the intervention of human agency, and which could not have been prevented by any amount of reasonable foresight, pains or care", e.g. flood, earthquake, frost.

Perils of the sea: This means "fortuitous accidents, or casualty of the sea". It comprehends winds, waves, storms lightning, icebergs, rocks, shoals, collision and in

(c) *Brenckelov S. Co. v. Boulton* (1875), L.R. 10 Q.B. 346.

(c1) *Alvion Steamship Corp. v. Gabban et al.* (1955) 1 All E.R. 457.

(d) *Clink v. Redford* (1891), 1 Q.B. 630.

(e) *Stag Lines Ltd. v. Board of Trade* (1950), 1 All E.R. 1105.

(e1) *Nath River Freighters Ltd. v. President of India* (1956) 1 All E.R. 50.

(f) *The Xentho* (1887), 12 A.C. 503.

general all loss or damage arising from the elements, and inevitable accidents, other than those of capture and detention. The loss need not be caused by extraordinary violence of the sea, e.g. striking a sunken rock in fair weather is included. Similarly, foundering by collision, even where the other ship is at fault is also included. Notice however (i) that the loss must be caused by a peril of the sea. Thus damage by rats which prevent a ship from sailing, is not covered, but if during the voyage, rats bore a hole, and sea water thereby damages the cargo, the cl. will cover the same (g). Similarly, direct injury to cargo by rats, is not covered. (ii) Further, ordinary wear and tear, caused by the normal action of wind or wave, is not included in the cl. It covers accidents, which may happen, not events which must happen. (iii) It does not include damage from war, confiscation of foreign courts, and barratrous action of master or crew. (iv) If the "peril" could have been avoided by reasonable care and diligence on the part of the master, the exception will not avail.

Fire: This means fire on board the ship. The shipowner must show that it occurred without any actual fault or privity on the part of the shipowner.

Barratry of Master and Crew: This means every wrongful act committed by the master or crew, to the prejudice of the charterer or owner, e.g. setting fire to the ship, scuttling, employing the ship on smuggling.

Enemies, pirates, thieves: "Enemies" means "King's enemies", i.e. subjects of government at war with the Government, to which a person is subject. "Pirates" means free booters of the sea. The term includes passengers who rise in mutiny, as well as rioters who attack a ship from the shore. It does not include persons who seize property for some public reason or purpose. "Thieves" does not include thefts committed by persons in employ of the ship or by passengers.

"Arrest and restraint of princes, rulers or people": This refers to loss or damage caused by political or executive acts, e.g. capture by an enemy during war, stoppage of neutral vessel for carrying contraband, embargo in times of peace. Restraint of people refers to municipal laws, e.g. prohibition by municipal rule against landing of cattle affected by foot and mouth disease (h).

"All other accidents or errors of navigation, etc.": This clause when included gives the widest protection, to the shipowner. It is, however, always strictly construed. It will not protect the shipowner's own negligence, e.g. employing a drunken master. It will also not protect a breach of the warranty of seaworthiness.

BILL OF LADING

Meaning: A bill of lading is a document acknowledging the shipment of goods, signed by or on behalf of the carrier and containing the terms and conditions upon which it has been agreed that they are to be carried. It is generally used for the carriage of goods on a "general ship", i.e. a ship which is used for the carriage of the goods of various merchants who may desire to have them conveyed by her and which is not employed for the carriage of a charterer's goods only. A bill of lading is also used even when a ship is chartered as a whole. If the charterer finds the cargo himself, the bill of lading is usually, though not always, a mere receipt for the goods given by the master. If the charterer takes the goods of others, the bill of lading is the contract between him and them. The following is a usual form of a bill of lading:

Form of Bill of Lading: "Shipped in good order and condition by _____ in and upon the good ship called the 'British Tar' whereof _____ is master for this present voyage, and now in the port of _____ and bound for _____ with liberty to call at any port on the way for coaling or other necessary purposes, fifty casks of wine being marked and numbered as per margin, and to be delivered in the like order and condition at aforesaid port of _____, the act of God, the King's enemies, fire, barratry of the master and crew and all and every other dangers and accidents of the seas, rivers, and navigation of whatever kind or nature soever excepted,

(g) *Hamilton v. Pondorf* (1887), 12 App. C. 518.

(h) *Miller v. Law Accident Ins. Co.* (1903), 1 K.B. 712.

unto or to his assigns, he or they paying freight for the said goods at £ per ton, delivered with prime and average accustomed. In Witness whereof, the master of the said ship, hath affirmed to bills of lading all of this tenor and date, one of which bills being accomplished, the others to stand void.

Dated, etc.

Weight, value and contents unknown".

Terms of bill of lading (B/L): These are generally the same as those contained in a charter party, though in an abbreviated form. What is stated above with regard to charter parties will, therefore, apply to bills of lading, with necessary modifications. Notice that it is the master who issues a B/L.

Mate's receipt

Where goods are taken on board in the course of a voyage or where it is not convenient to issue a B/L at once, "mate's receipts" are given. A "mate's receipt" is a mere acknowledgment of the receipt of goods. It is not regarded in law as a document of title to goods. It is afterwards exchanged for a B/L. If the master is not satisfied with the packing of the goods, he makes a remark to that effect on the receipt. It is then called a "dirty" or "foul" receipt. In other cases, it is called a "clean" receipt. A master can issue a B/L without production of a mate's receipt, if the goods are on board and he has no notice of other claims than those of the shipper. A shipowner is justified in issuing a B/L to the holder of a mate's receipt, if he has no notice at the time of any adverse claims. If a mate's receipt and a B/L get into different hands, however, the master is bound to deliver the goods to the person producing the B/L (i).

Position of Master

A master signing a B/L generally acts as the agent of the shipowner. If the ship is chartered, however, and the charter party creates a demise of the ship, the master becomes the agent of the charterer. Persons dealing with the ship, however, will not be affected by the above change of relations, unless they have notice of the change (j). Thus an indorsee for value of a B/L, without notice of the charter party, can hold the shipowner liable on the terms of the B/L. It would be otherwise, if he took with notice of the charter party. A master cannot sign a B/L, without the goods being actually on board. If he does so, he acts beyond his authority as agent of the shipowner, and the latter will not be bound by his act. In law, however, a B/L is *prima facie* evidence of the existence of the goods on board the ship. The shipowner therefore is bound to rebut the presumption. A B/L, however, is not even *prima facie* evidence of the quantity of the goods, if words like "quantity not known" are added (k).

As between the master and the consignors, a B/L is regarded in law as conclusive evidence of the receipt of goods on board the ship. The master can escape liability, only if he can show (i) that the holder of the bill knew at the time of receiving the same, that the goods were not on board, or (ii) that the misrepresentation was caused by the fraud of the shipper, holder or any other person claiming through him. A master cannot sign a B/L in terms different from those of the charter party, unless the charter party allows the same or unless special permission has been taken by the master.

Where a B/L states that the goods are shipped "*in good order and condition*", it is called a "*clean bill of lading*". The master is entitled in law to bind the shipowner by the use of such words and if the statement is incorrect, the shipowner will be liable in damages to any indorsee of the B/L for value without notice (l). The words, however, refer only to the apparent and external condition of the goods.

The master is bound to deliver the goods to the consignee or holder of the bill, on payment of freight. If the bill is in duplicate or triplicate, he must deliver the goods

(i) *Baumwoll v. Furness* (1893), A.C. 8.

(j) *Sandeman v. Scurr* (1867), L.R. 2 Q.B. 86.

(k) *New Chinese Antimony Co. v. Ocean S.S. Co.* (1917), 2 K.B. 664.

(l) *Brandt v. Liverpool Steam Navigation Co.* (1924), 1 K.B. 575.

to the holder of a B/L who first presents the same to him, provided he has no notice of conflicting claims at the time. If he has, he must file an inter-pleader suit. Where a B/L covers voyage by sea as well as carriage by land, it is called a "*through bill of lading*".

Transfer of Bill of Lading

A bill of lading is a "document of title to goods" and can be transferred by delivery, if it is a "bearer" document and by endorsement and delivery, if an "order" document, provided (i) goods are shipped on board and (ii) the voyage has not been completed or delivery made. The transferee of a B/L is therefore entitled to demand and receive possession and delivery of the goods. The transferee however had, at one time, no right to file a suit in his own name. The right has now been conferred on him by the Bills of Lading Act, 1856. He takes the bill, however, subject to all liabilities affecting thereto.

A bill of lading is *not* a "negotiable instrument" in the strict sense of the term. Thus its transferee acquires no better title than what his transferor had, although he may have taken the bill for value without notice. It is negotiable only in this sense that a *bona fide* transferee without notice will be able to defeat the vendor's lien or right of stoppage in transit where such right exists (*m*). Under the Indian Bills of Lading Act, 1856, it is expressly provided that though rights under a bill of lading vest in the consignee or indorsee thereof, the right to stop goods in transit, and the claim for freight against the original shipper is not affected thereby (sec. 2).

"Indian Carriage of Goods by Sea Act, 1924": Over and above the Indian Bills of Lading Act, 1856, mentioned above, bills of lading are also governed by another Act called "Indian Carriage of Goods by Sea Act, 1924". This Act is based on the English Carriage of Goods by Sea Act, 1924, and embodies in its schedule the rules made by the Brussels Convention as regards bills of lading. The Act applies to all ships carrying goods by sea from any port in India to any other port, in India or outside. It does not apply to charter parties and to contracts for carriage of particular goods (i.e. not ordinary commercial shipments made in the ordinary course of trade).

In cases of bills of lading to which the Act applies (i) there is no absolute warranty or seaworthiness. The carrier is only bound before and at the beginning of the voyage to exercise due diligence to make the ship seaworthy. He is not liable for loss or damage arising from unseaworthiness, unless caused by want of due diligence on the part of himself or his agent to make the ship seaworthy. The burden of proving that the loss was not so caused, however, is on the carrier.

(ii) Every bill of lading to which the Act applies shall contain a statement that it was issued subject to the Act.

(iii) On receipt of goods on board, the master, or other agent of the carrier, shall issue to the shipper a B/L containing the following particulars: (a) the leading marks necessary for identification of the goods as furnished in writing by the shipper before loading starts, provided they are clearly visible; (b) the number of packages or pieces, or their quantity or weight as the case may be, as furnished by the shipper in writing; (c) the apparent order and condition of the goods. Such a bill is *prima facie* evidence of the receipt of the goods so described by the carrier. The shipper is deemed to agree to indemnify the carrier against the above particulars turning out incorrect.

(iv) After the goods are loaded, the shipper has a right to demand a "*shipped bill of lading*" or a bill which acknowledges the shipment of goods on board and not merely the receipt thereof for shipment. If a bill of lading has already been issued, the shipper can exchange it for "*shipped bill of lading*".

(v) Written notice of loss or damage must be given to the carrier at the port of discharge, before or at the time of removal of the goods, and if the loss or damage is not apparent, within 2 days of the removal of the goods. In default, the carrier shall be deemed *prima facie* to have given delivery of the goods as described in the B/L.

(m) *Lickbarrow v. Mason* (1794), 5 T.R. 683.

(vi) If no suit is brought against the carrier for such loss or damage within one year of such delivery, the carrier shall be discharged from all liability for loss or damage to the goods.

(vii) The carrier is not liable for loss arising from (a) any act, neglect, or default of master or crew in the navigation or in the management of the ship; (b) fire, unless caused by actual fault or privity of the carrier; (c) perils, dangers and accidents of the sea or other navigable waters; (d) act of God; (e) King's enemies, restraint of princes, rulers and people and quarantine; (f) strikes, lockouts, riots or civil commotion; (g) saving or attempting to save life or property at sea; (h) wastage in bulk or weight or any other loss if caused by inherent vice of the thing itself; (i) insufficiency of packing or marks; (j) latent defects not discoverable by due diligence; (k) an act or omission of the shipper or his agent; (l) any other cause, arising without actual fault or privity of the carrier or his agents.

(viii) The carrier is not liable for loss or damage arising from "deviation" to save life or property or any reasonable deviation.

(ix) The carrier is not liable for loss or damage to goods above £100 in value per unit unless the nature and value of the goods concerned have been duly declared beforehand by the shipper and have been embodied in the bill of lading.

(x) Dangerous goods must be declared by the shipper beforehand; if not declared, the carrier may destroy them without being liable to compensate for the value. Even when declared, the carrier may discharge or destroy them, if they become a danger to the ship or cargo.

CHAPTER XIV

INSURANCE

MARINE INSURANCE

Definition: A contract of marine insurance is a contract of indemnity against loss incident to a marine adventure, accruing to ship, cargo, freight, or other subject-matter of a policy, during a given voyage or voyages or during a given length of time (Marine Insurance Act, sec. 1). It may thus be taken out in respect of ship, cargo, freight or any other subject of a marine adventure. It need not be limited to the actual loss sustained, as in fire insurance, but is generally based on value agreed to in advance, which may be greater or less than the risk involved. The consideration for the policy is called '*premium*'. The Insurers are called '*underwriters*'.

Marine insurance policies

These are of two kinds: (i) a "*company policy*" and (ii) a "*Lloyd's policy*". In a company policy, no brokers are generally employed. Further, the company takes the whole responsibility, however large, though it may re-insure the risk for its own protection. Far more common to the trade, however, are "*Lloyd's policies*". "*Lloyds*" are an incorporated society consisting of several members. It does other very useful work, besides insurance, e.g. collecting information about the movement of ships, classifying them, etc. In case of a "*Lloyd's policy*", an insurance broker must always be employed. If the rate of premium quoted by him is accepted by the assured, the broker prepares a "*Slip*" or "*Memo*" containing the material particulars of the proposed insurance, with the amount of the risk sought to be protected. The broker then proceeds to "*Lloyds*" office, and gets each member thereof to underwrite the risk to such extent as he desires, till the whole risk is made up. When the whole "*slip*" is filled and signed, the broker prepares a regular insurance policy. The underwriters of "*Lloyds*" sign the same in the respective amounts which they have underwritten. The policy is then stamped and handed over to the assured by the broker, in exchange of the premium.

The "Slip" or "Memo", when initialled by the underwriters, constitutes a binding contract according to mercantile code of honour and no underwriter can go back upon it without complete loss of reputation. In law, however, no binding contract of marine insurance arises till a policy of insurance properly made out and duly stamped is issued (see Stamp Act, sec. 7). The "slip", however, can be booked at for collateral purposes, e.g. to find out when the risk was undertaken or started.

Cover Note: This is a document often issued by underwriters to protect the subject-matter of insurance between the date of the contract of insurance and the actual issue of a marine policy. Such a note, however, is not regarded in law as either an insurance policy or an agreement to issue an insurance policy (n). It has been held, however, that if the cover note is properly stamped, a suit for specific performance can be founded thereon (o).

Insurable interest

No person can take out a marine insurance policy unless he has an insurable interest. A policy taken out by a person who has no such interest is void in law. A person is said to have an "insurable interest" when he is interested in a marine adventure and in particular, when he stands in any legal or equitable relation to the adventure or to any insurable property at risk therein, in consequence of which he may benefit by the safe arrival of the ship or may be prejudiced by its loss, damage or detention.

The following persons have been held to have "insurable interest": (i) shipowner; (ii) cargo owner; (iii) mortgagee to the extent of the sum due to him; (iv) mortgagor to the full value of the property; (v) Insurer; (vi) bottomry bond holder (see seq.); (vii) person advancing moneys for necessities of ship, to the extent of the advance; (viii) persons advancing freight, if freight is not recoverable in case of loss; (ix) master and crew can insure for their wages; (x) trustee or bailee; (xi) agent incurring personal liability; (xii) shippers and their agents.

An agent taking out a policy in his own name for a principal has no insurable interest on the goods to enable him to sue on the policy. But when such agent has incurred expenses on behalf of his principal, e.g. has paid freight, insurance premium and has incurred expenses as bailee for his principal, he has got an insurable interest in the goods and he can sue in his own name in respect of insurance policy taken by him on the goods (p).

Insurable interest must exist at the time the loss occurs. It may accrue during the pendency of the policy. It may accrue after loss even, if the policy includes the words "lost or not lost". Defeasible and contingent interest can also be insured, as well as partial interest.

The policy must be signed by the insurer and sealed, if the underwriters are a corporation. It must also contain (i) the name of the assured or his agent; (ii) the subject-matter and the risk insured against; (iii) the voyage or the period covered by the policy; (iv) the sum insured; (v) and the name of the underwriters. (vi) It must be properly stamped also. This is because of sec. 7 of the Stamp Act, which requires all policies of sea insurance to be stamped as required by law in absence of which no claim under such a policy can be enforced in a court of law. Contracts of marine insurance referred to in sec. 506 of the Merchant Shipping Act are, however, exempted from the operation of the sec. Thus a contract of marine insurance contained in a bill of lading is not bad because it is not stamped as a policy (q).

Kinds of marine policies

Various kinds of marine insurance policies are known: (i) An "interest policy" is a policy which shows that the assured has a specific local interest at risk, e.g. 100 bales of wool.

(n) Surajmall v. Triton Ins. Co., 52 Cal. 408.

(o) Bhugwandas v. Netherlands Sea & Fire, 14 A.C. 83.

(p) Ramji Karamsi v. Unique Motor Ins. Co., 52 Bom. L.R. 703.

(q) Reference 30 Cal. 565.

(ii) A "*voyage policy*" is a policy which covers a particular voyage. It is generally "at and from" one port to another.

(iii) A "*time policy*" is a policy which covers a specified period of time. Under law, it cannot be entered into for a period over a year. It may, however, contain a "continuation clause", providing that if at the end of the period, the ship is at sea, the policy will continue till the safe arrival of the ship at port of destination and for a reasonable time thereafter. If the risk attaches under the "continuation clause", a fresh policy, duly stamped, covering the period in question will be necessary before the assured can succeed.

(iv) A "*mixed policy*" is a combination of a "voyage" and "time policy".

(v) A "*valued policy*" is a policy which mentions the value of the subject-matter of insurance. In absence of fraud, the value is regarded as conclusive as between the assured and the insurer, except for purpose of ascertaining "constructive total loss".

(vi) "*Open*" or "*unvalued policy*": This is a policy where the value of the subject-matter is not mentioned but is required to be proved or assessed, in case of loss. It is generally rare.

(vii) "*Floating Policy*": This is a policy which mentions no particular ship or cargo but mentions only the amount for which the insurance is taken out, with a provision that the benefit thereof is to attach to ship or cargo "hereafter to be mentioned". As each shipment is made, the value and other necessary particulars are declared to the broker till the amount of the policy is written off.

(viii) "*Wager policy*", "*P.P.I. policy*": This is also called "interest or no interest policy". These are policies which are issued when the assured has no insurable interest in the subject assured and has no expectation of acquiring such interest at the time of the contract. "P.P.I." means "policy proof of interest". As such policies amount in effect to dispensing with all proof of insurable interest, they are regarded as purely gambling transactions and therefore void as wager. They are called "*honour policies*" also, because the trade recognises the binding obligation of such a policy. Policy made "without benefit of salvage" is also in law a wagering policy, except where there is no possibility of salvage. It has been held in England that a "P.P.I. policy", is void even though the assured had, in fact, an insurable interest when the policy was signed and issued (r).

Premium: The underwriter is not bound to issue a policy unless the premium is first paid by the assured. Generally it is paid to the broker, who is responsible for accounting for the same to the underwriter. A policy which acknowledges receipt of the premium is, in law, in absence of fraud, conclusive evidence of payment of such premium, as between the underwriter and the assured, although the broker has, in fact, not accounted for the premium to the underwriter. It is not conclusive, however, as between the broker and underwriter.

The broker, in marine insurance, is generally regarded as the agent of the assured. He has a lien on the policy for the premium, and his brokerage and other charges. It is a general lien, under sec. 171 of the Contract Act, and it extends to cover a general balance of insurance account as between him and the customer. In India, however, the practice of employing brokers is at a discount and in Indian commercial usage, he does not occupy the same position as a broker in London does, with regard to a Lloyd's marine policy (Barwell).

Assignment of policy: A person insuring his interest in a marine adventure is always entitled to assign the policy unless the terms thereof forbid a transfer. The assignment may be by endorsement on the policy or in any other customary manner, e.g. if the policy is endorsed in blank, by delivery (s). The assignment may be before or after the loss has occurred. It enables the assignee to sue in his own name on the policy (t).

(r) Re London County, etc. Office (1922),
2 Ch. 67.

(s) Sec. 130A, Transfer of Property Act.
(t) Sec. 135A, Ibid.

The same defences, however, are open against the assignee as were available against the original assured, e.g. non-disclosure of material facts.

Notice however that if the assured has parted with or lost his interest in the subject-matter of insurance, he cannot assign the policy, unless, he has, before or at the time of parting of his interest, expressly or impliedly agreed to assign the policy (u). Similarly, if the assured had no interest before loss, no assignment could be made by him.

Good faith and misrepresentation: A contract of marine insurance is contract of "abundant good faith", i.e. "*uberrime fidei*". The assured therefore is (a) bound to communicate to the underwriters, every material circumstance known to the assured, which would affect the mind of a prudent underwriter in fixing the premium or undertaking the risk. (b) He must not also be guilty of any misrepresentation to the underwriter or his agent, while negotiating the policy. A breach of either of these two requirements makes the policy void.

Instances of (a) are the following: (i) that the vessel is overdue; (ii) that it is damaged; (iii) that it is lost; (iv) concealing the nationality of the assured, where such nationality is of importance (v). (v) The fact that the goods carried on the ship are grossly over-valued when the ship is insured (w). An assured, however, is not bound to disclose, what the underwriter knows or should know, e.g. (i) a general trade custom; (ii) speculation as to war; (iii) a tempest.

Warranties

A "warranty", in marine insurance, has a different meaning from that in the "Sale of Goods Act". A "warranty" here means, a term the breach of which entitles the insurers to avoid the policy altogether (x). It is therefore on the same footing as a "condition" in the "Sale of Goods Act". If such a term is broken, the whole policy becomes void and inoperative. The extent of the loss caused thereby as well as the materiality of the risk involved, are both immaterial in this connection. Further, the fact that the breach arises owing to events beyond the control of the warrantor is also no excuse. A "warranty" may be (a) "express" or (b) "implied".

"Express warranties" usually are: (i) to call on a given day; (ii) that the vessel is safe on a particular day; (iii) that the ship will sail with convoy, i.e. with government armed escort; (iv) that the ship is neutral and shall continue to be so, during the pendency of the risk and further that it shall carry proper papers; (v) that the goods are neutral and shall continue to be so, during the continuance of the voyage.

"Implied warranties" are those which are implied by law in every contract of marine insurance, unless, by express words, they are excluded. They are: (i) in a voyage policy on a ship, that the ship is seaworthy at the commencement of the voyage, for the particular adventure and if the voyage is by stages, also at each stage. If the ship is in port, the warranty extends to this, that the ship is fit to encounter the ordinary perils of that port. There is no such warranty in a time policy. (ii) In a voyage policy on goods, that the ship is seaworthy at the commencement of the voyage and is also reasonably fit for carriage of the particular goods. There is no such warranty in a time policy. (iii) That the adventure is a lawful one.

There is no implied warranty of the nationality of the ship or that it shall not be changed. Further, in a policy on goods or other moveables, there is no implied warranty that the goods or moveables are seaworthy. Notice further that non-compliance with a warranty is excused only if (i) by change of circumstances, it does not apply or (ii) if compliance therewith is rendered unlawful by legislation.

Form of Marine Policy

S.G. £. BE IT KNOWN THAT A and or as Agents as well in his own name as for and in the name and names of all and every other person or persons to whom

(u) Sec. 130A, Ibid.

(v) Associated Oil Carriers Ltd. v. Union Ins. Society of Canton (1917), 2 K.B. 184.

(w) *Ionides v. Pender* (1874), L.R. 7 Q.B. 531.

(x) *De Hahn v. Hartley* (1786), 1 T.R. 343.

the same doth, may or shall appertain in part or in all doth make assurance and cause himself and them, and every one of them, to be insured *lost or not lost* (1) *at and from* (2) London. Upon any kind of goods and merchandises, and also upon the boat, tackle, apparel, ordnance, munition, artillery, boat, and other furniture, of and in the good ship or vessel called the "Mary", whereof is master under God, for this present voyage, John Smith or whosoever else shall go for master in the said ship, or by whatsoever other name or names the said ship, or the master thereof, is or shall be named or called; beginning the adventure upon the said goods and merchandises from the loading thereof aboard, the said ship upon the said ship, etc. and so shall continue and endure, during her abode there, upon the said ship, etc. and further, until the said ship, with all her ordnance, tackle, apparel, etc. and goods and merchandises whatsoever shall be arrived at Melbourne upon the said ship, etc. *until she hath moored at anchor twenty-four hours in good safety*, (3) and upon the goods and merchandises, until the same be there discharged and safely landed, And it shall be lawful for the said ship, etc. in this voyage to *proceed and sail to and touch and stay*, (4) at any ports or places whatsoever on the West Coast of Africa without prejudice to this insurance. The said ship, etc. goods and merchandises, etc. for so much as concerns the assured, by agreement between the assured and assurers in this policy, are and shall be valued at: (5) *Touching the adventures and perils which we, the assurers, are contended to bear and to take upon us in this voyage; they are of the seas, men of war, fire, enemies, pirates, rovers, thieves, jettisons, letters of mart and countermart, surprisals, takings at sea, arrests, restraints, detentions of all kings, princes and people of what nation, condition, or quality soever, barratry, of the master and mariners, and of all other perils, losses and misfortunes, that have or shall come to the hurt, detriment or damage of the said goods and merchandises and ship, etc. or any part thereof: And in case of any loss or misfortune it shall be lawful to the assured, their factors, servants and assigns, to sue, labour and travel* (6) for, in and about the defence safeguards, and recovery of the said goods and merchandises and ship, etc. or any part thereof, without prejudice to this insurance; to the charges whereof, we the assurers will contribute each one according to the rate and quantity of his sum herein assured, And it is expressly declared and agreed that no acts of the insurer or insured in recovering, saving or preserving the property insured, shall be considered as *waiver or acceptance of abandonment*. (7) And it is agreed by us, the insurers, that this writing or policy of assurance shall be of as much force and effect as the surest writing or policy of assurances heretofore made in Lombard Street or in the Royal Exchange, or elsewhere in London And so we, the assurers are contended and do hereby promise and bind ourselves, each one for his own part, our heirs, executors and goods to the assured, their executors, administrators, and assigns, for the true performance of the premises confessing ourselves paid the consideration, (8) due unto us for this assurance by the assured at and after the rate of

In Witness Whereof we, the assurers, have subscribed our names and sums assured in London.

N.B.—Corn, fish, salt, fruit flour and seed are warranted free from average, unless general or the ship be stranded; sugar, hemp, flax, hides and skins are warranted free from average under five pounds per cent; and all other goods, also the ship and freight, are warranted free from average under three pounds per cent, unless general or the ship be stranded. (9)

Notes on clauses

(1) "Lost or not lost": Marine Insurance can be effected while the goods are at sea. In such cases the parties have no means of knowing whether the subject-matter of insurance is intact or not. In order to obviate the difficulty which may be created by a possible loss of the subject-matter before the insurance is effected, these words are introduced. They give a retrospective protection to the assured from the time the voyage started. The assured therefore can recover though the subject-matter was already lost, at the date of insurance. So also the underwriter can recover the premium under similar circumstances. Of course, the assured cannot recover, if he was aware of the loss at the time the policy was effected. The protection of the above words however does not apply to "floating policies".

(2) **At and from:** These words fix the time when the risk is to begin. If the word is "from" merely, the risk will begin when the ship starts on the voyage. If the words are "at and from", the risk dates from the time the contract is concluded, provided the ship is in safety at the time. If the ship is not in safety at the time, the risk will be on her arriving in good safety at the port of departure. In both cases, there is an implied condition that the ship shall sail within a reasonable time. If unreasonable delay is caused, the insurers are discharged from the policy. If the place of departure is mentioned, the insurers are discharged if the ship does not sail from such place. Generally the insurer is not liable for loss during loading and unloading. If it is intended to make him liable, the words "including risk of craft to and from vessel" are added.

(3) **Until she has moored, etc.:** These words specify the time of the cessation of the risk. The risk in case of a ship continues till she has moored in safety for a particular time and in case of goods, till they are safely landed. The goods must be landed in the customary manner and within a reasonable time after arrival. If they are not so landed, the risk ceases. If use of lighters is customary, risk continues till the goods are safely landed by lighters.

(4) **"Touch and Stay":** This is called the "touch and stay" clause. It gives permission to the assured to call at stated ports for stated purposes and for stated time, during the course of the voyage. In absence of such a cl., the ship cannot deviate from its usual or agreed course.

"Deviation" means "going out of the proper course as agreed or as prescribed by custom, between the two termini of the voyage". Instances of deviation are: (i) going to a port not named in the policy or justified by custom; (ii) visiting ports in different order than laid down in the policy; (iii) where several ports are mentioned, taking them in a non-customary order; (iv) staying to trade at a port, where no such liberty is granted; (v) calling at places for purposes outside the scope of the voyage. (vi) Improper delay in prosecuting the voyage is also "deviation". A voyage must be prosecuted with reasonable diligence. If it is not so prosecuted the insurer is discharged from liability, because then it becomes a new voyage. Notice that if after commencement of the risk, the destination of the ship is voluntarily changed, it is not "deviation". It is a change of voyage and the policy does not avail.

Deviation is excused, however, in the following cases: (i) if allowed by the policy; (ii) if caused by circumstances beyond the control of the master or his employees; (iii) if reasonably necessary to comply with a warranty; (iv) to ensure safety of the ship or the subject-matter insured; (v) to save human life or a ship in distress, when loss of life is feared; (vi) if it is caused by the barratrous conduct of the crew, if barratry is a peril insured against. Notice that deviation for saving property is not excused (y).

Once the cause of deviation is removed, the ship must resume her usual course and prosecute the voyage with reasonable diligence. The result of an unjustifiable deviation is that the whole contract is discharged, even though the loss occurs after the ship has returned to the usual course and the deviation has not increased the risk.

(5) **"Accepted perils":** This is a counterpart of the "excepted risk" clause in a charter party (see ante). The insurer thereby undertakes to indemnify the assured for all loss caused to him by any of the perils mentioned therein. Some items not considered before are dealt with here:

"Jettison": This means throwing overboard cargo or tackle to lighten the ship *bona fide* and in an emergency. If done on account of the inherent vice in the thing itself, it will not be covered. It does not also cover goods carried on deck. The insurer is not liable to indemnify for such goods, if thrown overboard.

"Letters of Mart and Countermart": These are commissions or letters of authority granted by Government, empowering the holders to make reprisals on enemy shipping in answer to attacks by the enemy on its own ships.

"All other perils": This will not include any peril, but only analogous perils (z).

(y) *Scaramanga v. Stamp* (1880), 5 C.P.D. 295.

(z) *Samuel & Co. v. Dumas* (1924), A.C. 431.

(6) **"Sue and labour clause"**: This cl. means that the assured, in case of loss, must act as uninsured so far as saving of property from loss is concerned, in case the risk attaches. If the assured acts in such a manner, the insurers thereby undertake to contribute to the expenses. Notice, however, that "general average" and "salvage" are not included in the cl. "Sue and labour clause" only covers damage due to accident or casualty (z1): e.g. it does not cover expenses incurred by assured for repairing damage to subject of insurance by reason of an inherent vice therein (z2).

(7 & 8) **Waiver clause**: This means that in case of loss, the work of saving property, if undertaken by any of the parties, will not disentitle that party from enforcing his rights with regard to the policy. Such work will not be construed as "waiver" or "acceptance of abandonment" (see seq.).

(9) **N.B.**: This is also called 'memo'. Its object is to protect insurers from loss on goods, which are peculiarly liable to damage on a sea voyage and certain small losses, which must inevitably occur. For this purpose goods are divided into several classes (see cl.). "Warranted free from" means that the insurer is not liable for such loss.

In class (i) the exemption from liability is in respect of partial loss or damage, unless (a) the loss is a "general average loss" or (b) is caused by the ship stranding. "Stranding" means the ship touching the sea bottom or anything connected therewith, whereby it is detained in the voyage for an appreciable length of time. The grounding must be accidental and unusual in place and manner and the ship must remain hard and fast on the obstruction. For "general average loss" see seq.

In class (ii) the insurer is exempted from liability unless damage to the goods amounts to £5 p.c. or over.

In class (iii), the insurer is exempted from liability for loss not exceeding £3 p.c. unless (a) the loss is "general average loss" or (b) the ship is stranded. Notice that if loss exceeds the fixed percentage, the insurer is liable for the whole loss and not merely for the excess. Further, if the cargo is separately valued, or is consigned as "separate packets" or "series", each packet or item of the "series" will be regarded as an independent single unit.

Other clauses

Various other cls., when necessity requires their introduction, are also incorporated in a marine policy. Some of these are as follows:

(i) **"F.C. & S. clause"**: This cl. provides that the subject of insurance, is "warranted free from capture and seizure", i.e. the insurer will not be liable for loss caused to the subject by capture or seizure by an enemy. The cl. is usually introduced during war. The onus however is not on the assured to show that the loss was caused by perils other than that of capture, but on the insurer to show that it was in fact caused by capture, etc. Under the cl., the insurer's liability ceases on capture of the vessel, though the actual loss occurs subsequently, by any of the perils insured against (a).

(ii) **F.P.A. clause**: This cl. provides that the subject of insurance is "warranted free from particular average". It exempts the insurer from all liability for particular average, except in certain cases, e.g. unless the vessel is stranded, sunk, burnt or damaged in collision. Salvage charges and charges incurred under the "sue and labour" cl. are not included.

(iii) **F.A.A. clause**: Under this cl., the insurer is exempted from liability, both for particular average and general average, except in certain cases.

(iv) **Running down clause**: Ordinarily a marine policy does not cover damages payable by the assured on account of his ship colliding with another. Hence this is included. It covers damages payable to a ship which suffers by reason of the insured ship colliding with another ship, which in turn collides with the first ship.

(z1) British and Foreign Marine Ins. Co. v. Gaunt (1921), 2 A.C. 47.

(z2) Berk & Co. Ltd. v. Style (1955), 3 All E.R. 625.

(a) Anderson v. Martin (1908), A.C. 334.

(v) "**Inchmaree clause**": This cl. is so called because it came to be introduced by reason of the decision of the Court in respect of a ship called "**Inchmaree**" (b). In this case, while water was being pumped into the boilers of a ship at anchor, off shore, it was forced back by reason of a valve being closed and thus disabled the ship's pump. It was held by the House of Lords, that the damage was not covered by "perils of the sea". Under the cl., certain losses caused (i) by the negligence of the master, the mariners, engineers and pilots, during loading or unloading or (ii) through explosions, or bursting of boilers or (iii) through latent defect in machinery or hull are covered.

Loss: Rule of "**proxima causa**"

Though loss may be caused to the subject-matter of insurance by any of the "accepted perils", such loss is not recoverable by the assured from the underwriter, unless the "loss" arises "proximately", i.e. immediately, from any of the accepted risks. This is called the *rule of "proxima causa"*, which is a special rule applied in marine insurance for assessment of damage. In order to recover loss under a marine policy, the loss (i) must have arisen from any of the "accepted perils" and (ii) the "peril" must be the proximate, i.e. direct cause of the loss.

Thus where a ship, which was insured against "hostilities", ran on a sunken wreck of another vessel, torpedoed by an enemy submarine, which happened to be lying at the place of the accident, it was held that the insurer was not liable for the loss, as "hostilities" were not the "proximate cause" of the loss but the accident of the sunken vessel, lying at the place where it lay (c). On the other hand, when an enemy had purposely sunk a vessel at the entrance of a port, in order to damage vessels entering therein, it was held that the loss was recoverable, being covered by a similar cl. as the above, in the policy (c). Similarly, where a cargo of oranges was insured, free from particular average, unless caused by collision and the ship having collided and put into port for repairs, the oranges were taken on lighters and then reloaded, it was held that the damage caused to the oranges thereby, could not be recovered under the policy, as the "proximate cause" of the damage was not "collision", but the unloading and reloading of the oranges (as aforesaid) (d).

"Proximate" however does not mean the "nearest in time". As Lord Shaw said in *Leyland Shipping v. Norwich Union* (1917), 1 K.B. 837, "the cause which is truly proximate is that which is proximate in efficiency". Lord Simon called it "the effective or predominant cause" in a recent English case (d1). The efficiency of a cause may have been preserved, though other causes may have in the meanwhile sprung up. If the ultimate event is the result of such an efficient cause, it will be regarded as the "proximate cause", though not proximate in point of time.

In the above case a ship which was "warranted free from all consequences of warlike operations", was seriously injured by an enemy torpedo at sea. It was brought to port however and safely anchored. The weather subsequently became rough and the vessel, straining, broke its back and became a total loss. Held, the efficient cause of the loss being warlike operation, the underwriters were not liable.

Loss of subject-matter of marine insurance may be either (i) *partial* and (ii) *total*. Total loss may be either (a) *actual total loss* or (b) *constructive total loss*.

Actual total loss

This occurs (i) when the subject-matter is actually destroyed or irreparably damaged.

(ii) Where the assured is irretrievably deprived of it, e.g. where the ship, though existing, becomes a bundle of planks, and thus ceases to be a ship.

(b) *Thomas & Mercy Ins. Co. v. Hamilton* (1887), 12 A.C. 484.

(c) *William etc. & Co. v. North of England, etc. Asso.* (1917), 2 K.B. 527.

(d) *Pink v. Fleming* (1890), 6 Asp. M.L.C. 544.

(d1) *Yorkshire Dale Steamship Co. v. Minister of War Transport* (1942), 2 All E.R. 6.

(iii) Where goods have ceased to exist in such condition or form, as to assume the denomination under which they were insured, e.g. long-staple Egyptian cotton, so damaged by sea water, that it cannot be sold in the market as such.

(iv) Where the subject is lost to the owner by a valid decree of a competent Court, in consequence of a peril insured against, e.g. being condemned as lawful prize.

(v) Where the ship is missing and is notified as such in Lloyd's Register. Notice that even if the ship is restored to the owner after action, this will not debar him from recovering as on an actual total loss.

Constructive total loss

This occurs when the subject-matter of insurance is not destroyed in fact, but is treated as destroyed, by a rule of law. This occurs (i) where the subject of insurance is reasonably abandoned, on account of its actual loss being inevitable, e.g. abandoning a ship on fire in mid-ocean.

(ii) Where the subject cannot be preserved from actual loss, except by an expenditure which will exceed its value when restored or repaired, e.g. where a ship, sunk in deep water, cannot be raised without expenditure in excess of its value; where a ship is so damaged that the cost of repairs will exceed its repaired value; where goods are so damaged, that the costs of reconditioning them would be greater than their value on arrival; where loss of freight cannot be prevented except at a cost exceeding the amount of freight.

(iii) Where the assured is deprived of the ship or goods by a peril insured against and it is unlikely that he would recover them, e.g. cargoes taken to neutral ports in enemy vessel during war. The assured in such case is bound to show that at the date of commencement of the action, the balance of probabilities was that the subject will not be recovered.

(iv) Where goods are insured "at and from" a certain port to another, and by a peril insured against, the adventure or voyage is frustrated (e). Thus when British ships carrying cargo from Argentina to Hamburg were, on declaration of war between Germany and England, directed by French warships and the British Admiralty to British ports, and had their cargo warehoused there, it was held that the owner of the cargo could claim on the basis of "constructive total loss".

Ship's protest: This is necessary in case of "actual total loss", provided any of the crew is saved. It is to be sworn before a notary public and contains a detailed account of the casualty, along with a claim by the assured under the policy. It must be accompanied by a bill of lading or invoice, showing that the goods were *bona fide* on board. The policy must also be produced. It is generally retained by the insurers, after payment of the loss. The object of the protest is to exonerate the master and mariners or persons making the protest from any charge of improper, illegal or negligent conduct.

Notice of abandonment: This is a notice by the assured to the insurers that he abandons all interest in the subject of insurance to the insurers, on account of the damage caused to it by an "accepted peril" and would claim against the insurers in respect thereof, on the basis of a "constructive total loss".

This notice is required by law to be given to the insurers, when the assured desires to claim against them, on the above basis. If not given, the assured can claim only on the basis of partial loss. It must be given with reasonable diligence after receipt of reliable information as to loss, reasonable time for inquiry being given. It must be given, however, at the earliest possible opportunity by the owner or his properly authorised agent. It need not be in writing. If the insurer accepts the notice, he becomes bound to pay on the basis of "constructive total loss". He is, however, not bound to accept the notice. His refusal does not prejudice the assured, who will then be required to prove his claim of "a constructive total loss" in a Court of Law.

(e) British & Foreign, etc. Co. v. Sanday & Co. (1916), 1 A.C. 650.

The effect of such "notice" is that thereafter all rights of the assured in the subject of insurance, pass to the insurer, including freight subsequently earned. The insurer in fact stands after notice, in the position of the assured, as regards the subject-matter of the policy. The transfer relates back to the date of the accident. If, therefore, after payment of loss on the above basis, the vessel arrives safe, it is treated as abandoned and becomes the property of the insurer.

Settlement of losses: This is called "*adjustment of losses*" also. It is generally effected through brokers. The rules employed are as follows:

(a) In case of ship, (i) if loss is partial, the insurer will pay the cost of repairs, less customary deduction. This works out at 2/3rds of the expenditure, 1/3rd being allowed for increased value, except in case of first voyage. (ii) If the loss is total, the insurer will pay the insured value, if the ship is valued in the policy, and if unvalued, the full insurable value of the ship, at the commencement of the voyage (including stores, outfit, machinery, coal, etc.).

(b) In case of goods, (i) if the loss is total, the insurer will pay the valued amount, if the goods are valued, or their insurable value, if they are unvalued. Insurable value means, the cost, along with the expenses of shipping and insurance charges. (ii) If the loss is partial and the goods are valued, the insurer will pay such proportion of the insurable value of the goods as the part bears to the whole. If they are unvalued, he will pay the insurable value of the goods lost.

Notice that the assured can also recover from the insurer, any "general average expenditure" he has incurred, or any "general average sacrifice" he has suffered without enforcing his claim for contribution against the other parties concerned. If the assured is liable to pay any "general average contribution", he can claim to be indemnified by the insurer in respect thereof, according to proportion and subject to the terms of the policy. The insurer, however, is not liable to pay for general average contribution, if it is not incurred in avoiding a peril insured against. Unless the policy provides to the contrary, the insurer is liable for successive losses, even though the total amount may exceed the sum insured. A partial loss, however, followed by total loss can only be regarded as total loss (f).

Subrogation

This is a right by which the underwriter, on paying or settling a loss, becomes entitled to all the rights of the insured, in or with regard to the subject of insurance as from the time of the casualty causing the loss. Thus, if after paying for a total loss, the ship is recovered, the insurer becomes the owner of the ship. He becomes also entitled to any right of "general average contribution" which the insured had.

The right, however, extends only to the extent of the value insured. Thus if the subject is insured for half its value, the insured retains his full right in the other half. Where the insurer pays for a partial loss he acquires no interest in the subject-matter insured, but he is thereupon subrogated to all rights and remedies of the insured person as from the time of the casualty causing the loss, in so far as the insured person has been indemnified by such payment for the loss (g).

"Particular average"

Wherever damage is done by accident or otherwise to property which is involved in a marine adventure, and the damage is not one which is suffered for general benefit, it is called "particular average" (P/A); e.g. damage to cargo by sea water, damage to ship in the shape of loss of anchor or wreck of a propeller. It may be on ship, cargo or freight.

The rule with regard to such losses is that they lie where they fall. There is no right of extraordinary compensation with regard to them. Such loss is recoverable from

(f) *British & Foreign, etc. Co. v. Wilson Shipping Co.* (1921), 1 A.C. 188.

(g) Sec. 135A, Transfer of Property Act.

the insurer if (i) it is so provided in the policy, and (ii) if it is caused by a peril insured against. It must, however, be fortuitous or accidental.

General average

"General average" (G/A) means "loss which occurs where any extraordinary sacrifice or expenditure is voluntarily and reasonably made or incurred, in time of peril, for the purpose of preserving property involved in a common adventure". It is also defined as "loss caused or directly consequential" on a "general average act". The rule with regard to such loss is that it must be borne rateably by all the parties interested in the common adventure. General average may consist of (i) a sacrifice of property or (ii) incurring of certain expenditure.

The essentials of a "general average sacrifice" are as follows: (i) It must be made to avoid a danger common to all interests. (ii) It must be reasonably and prudently made. (iii) It must be of an extraordinary nature. (iv) There must be necessity to incur some sacrifice. (v) It must be voluntary and not accidental. (vi) It must be really and truly a sacrifice, not throwing away something which has already become useless, e.g. a broken mast. (vii) The ship, cargo or some portion thereof must have been actually saved thereby. (viii) The danger must not have arisen through the default of the interest demanding "general average contribution", except in case of loss brought about by the inherent vice of the thing. (ix) The loss must be the direct result of the "general average act".

Instances of *G/A sacrifice* are: pouring water into the hold to extinguish self-ignited coal and thus causing damage to other cargo of coal; landing or jettisoning cargo to lighten ship in distress; voluntary stranding of the ship, in order to avoid a wreck; damage to cargo by scuttling the ship to avoid fire. The essentials of a "general average expenditure" are also similar. The occasion to incur such expenditure must be extraordinary, the expenditure also must be reasonable and prudent, and some definite benefit must have resulted by incurring the same.

Instances of *G/A expenditure* are: expenses of putting into a port of refuge to save the ship or cargo; out-of-pocket expenses incurred and commission paid to raise funds at the port of refuge; expenses incurred in taking vessel to its destination, with help from outside, in the shape of a tug or a tow, where actual unloading and warehousing the cargo and thereafter repairing the damage and reloading at the port of refuge would have been more expensive (such expenses are called "substituted expenses"). Notice, however, that hiring a tug in order to hasten voyage during war time has been held not to be a *G/A expenditure*, when the ship is protected by war risk insurance.

Adjustment of G/A: Generally the rules of the port of discharge regulate the amount which is payable for G/A. Underwriters frequently agree to pay G/A "as per foreign statement". When so agreed, such statement is binding on them. *York-Antwerp Rules of 1924* are a set of comprehensive rules framed by certain European powers for assessing liability for G/A contribution.

Sometimes when the general average contribution is large, the shipowner collects the G/A from cargo owners beforehand, and deposits the collection with two trustees. This is called "*G/A deposit*". The shipowner in exchange gives a "deposit receipt". "*Average bond*" is a bond taken by the shipowner from the cargo owners, when releasing their cargo, that they will pay their shares of G/A.

"General average contribution": The rule of maritime law is that all who have benefited by the "general average act" must share the loss or the expenditure, i.e. they must all contribute to the same. This liability extends to owners of the ship, the cargo and the freight but not to wages of seamen. Contribution is levied in proportion to the value of the thing benefiting by the G/A act. Goods landed for safety (and not for lightening) are not liable to contribute. Where property of a third party is damaged by a G/A act, e.g. causing damage to a pier or dock, voluntarily, for purpose of safety, all interests must contribute towards the damages payable. The rule that there can be no contribution between joint tortfeasors, does not apply to such a case.

Notice that the master has a right to retain the cargo till G/A contribution in respect of the same has been paid. Notice further that amount made good as G/A, has itself also to contribute to G/A. The owners of the goods lost by G/A act are treated as if these goods were saved. G/A on their goods therefore is also calculated and deducted from the amount payable to them.

Proof of claim: A term in a marine insurance policy that "no claim shall be admitted unless properly made and proved within forty days from the date hereof" is not to be regarded as a condition which must be rigidly fulfilled before a claim can be successfully made. If the assured has substantially complied with the term, with all reasonable diligence, he is entitled to succeed (h).

"Bottomry": This is a transaction in which the master of a ship, pledges or hypothecates the ship and/or cargo and/or freight by means of a bond, in order to raise money for the benefit of the ship and/or cargo. "Bottomry bond" is an instrument in writing executed by the master binding him to repay the money advanced, within a limited time after the safe arrival of the ship at its destination and in the meantime assigning the ship, freight and/or cargo as security for the same.

The essential elements of a bottomry bond are: (i) the repayment must be conditional on the safe arrival of the ship. (ii) There must be necessity to raise the loan. This is the "touchstone". The ship must be in distress, the master must have no credit, and the money must be required for necessary purposes. (iii) The master must have made all possible efforts to raise money otherwise, short of selling the cargo. (iv) The bond must be given, for loans advanced to the ship and not for the master's personal debts.

The rights of the holder of such a bond are: (i) It gives a right to him to enforce his claim against the ship by an action *in rem*, in the Admiralty Court. (ii) His claim ranks preferentially to a mortgagee, though not to wages and salvage. (iii) The last holder of a bottomry bond, ranks first and the first last, when there is a competition between holders of different bottomry bonds.

"Respondentia": This is hypothecation of cargo only. The master can do so, only if overriding necessity arises. He must, however, communicate with the cargo owners beforehand, if it is possible. The owners of cargo covered by such a document are entitled to an indemnity from the shipowner, in case the bond is enforced.

Salvage: This is reward allowed by law to persons who save ship, apparel, cargo or freight, from shipwreck, capture or similar jeopardy. In order to earn salvage however (i) the services must have been voluntary; (ii) there must be peril; (iii) some skill and enterprise must have been shown. (iv) The services must have been beneficial.

The rights of a salvor are: (i) he has a maritime lien on the property saved. (ii) He ranks first of all, amongst claimants against the property. (iii) The cargo owners are liable for salvage in proportion to other property saved. (iv) The amount awarded is divisible between owner of ship, master, crew and officers of the salving vessel.

Return of premium: If the contract of insurance was induced by fraud or misrepresentation, the premium is not returnable at law, on the insurer avoiding the policy. In certain cases, however, it is returnable. These are:

(i) Where the consideration for the premium has totally or partially failed. In the last case, apportionment is made. Thus where the subject or an apportionable part thereof is never subjected to the risk, e.g. if the insured vessel has already arrived safely at the time the contract is entered into, premium paid will be refundable. It will also be refunded, if the policy is void or is avoided by the insurer from the commencement of the risk.

(ii) Where the assured had no insurable interest at any time during the currency of the risk, provided the contract was not by way of wager.

(iii) Where the assured *bona fide* over-assures, on an unvalued policy, proportionate premium is returnable.

(iv) If the assured over-insures by double insurance, *bona fide*, and not knowingly.

Re-insurance: Insurers who undertake a risk generally insure their own risk, either wholly or partially with other insurers, in order to protect themselves. This is called "re-insurance". The relations between the insurer and the re-insurer are governed by the ordinary rules of insurance. The original insured however has no right or interest in such re-insurance, unless the policy otherwise provides.

Double insurance: This arises where the assured has *bona fide* effected two or more policies to cover the same interest and the total sum exceeds the amount of indemnity payable to the assured in case of loss. In such a case, the assured can recover under any one or more of the policies taken out, provided he does not recover more than the amount of the indemnity due to him. If the assured recovers any sum under any one of the policies, he must give credit for the amount against the value, in case of valued policy and against full insurable value in case of an unvalued policy. If he recovers more than his due, he holds the balance as trustee for the insurers, according to their respective rights *inter se*. The insurers between themselves are bound to contribute to the loss in proportion to the amount for which they are each liable. If more than one's share is paid, a suit for contribution is maintainable.

NON-MARINE INSURANCE POLICIES

Three classes of insurance policies are known, besides marine policies. They are (a) personal insurance, including life, accident and sickness insurance, (b) property insurance, including fire, burglary, fidelity and other insurance of property, and (c) liability insurance including motor vehicle and employees' liability and other liability insurances. There may be combined policies also, including more than one risk. Of these kinds of insurances, fire and life insurances are most important. They are considered below :

FIRE INSURANCE

Definition: This is a contract whereby one party undertakes to indemnify another, against the consequences of fire, happening within an agreed period, in return for payment in lump or by instalments.

Insurable interest

The assured must be liable to suffer some pecuniary loss by fire, i.e. he must have an insurable interest in the subject, before a fire policy can be regarded as valid. The following have been held to have "insurable interest": (i) owner, (ii) mortgagee, (iii) warehouseman as regards customers' goods; (iv) trustee or executor; (v) a person under an agreement of purchase; (vi) a common carrier; (vii) a pawn broker; (viii) a commission agent having interest in the agency; (ix) tenants who are liable to pay rent after a fire; (x) insurer himself; (xi) a person in possession, or (xii) even a finder. The interest may be legal or equitable or may arise under a contract of purchase or sale. Interest must exist at the time the insurance is effected. Insurable interest must exist at the date of the loss.

Procedure: Generally a broker is employed. Such a broker in India is generally the agent of the insurer. A receipt of premium signed by such broker, protects the party till a policy is issued or the risk is declared. It is called a "cover note" or "interim protection note". In England such a "note" offers full protection to the assured, till the policy is actually issued (i). The policy, when issued, supersedes the note. Sometimes a "slip" initialled by the broker and containing the main terms of the contract of insurance is issued. This also has been held in England to be a sufficient contract of fire insurance, though no premium has been paid (j).

(i) Thomson v. Adams, 23 Q.B.D. 366.

(j) Re Colman's Depositors etc. Ltd. (1907), 2 K.B. 798.

The law in India, however, is otherwise. A "slip" or "cover note" issued in respect of a "fire policy" is not effective in India. This is because of the general "exemption" under Act 47 of the Stamp Act (k). They can be used only for securing specific performance of a contract to issue a fire policy. The policy terminates on the date fixed. Sometimes, "days of grace" are provided for, within which the policy can be renewed. If so, loss occurring during the period will be covered.

Disclosure

A contract of fire insurance is also a contract of "abundant confidence". The person intending to insure usually fills in a "proposal form". If the answers to the questions in the proposal form are untrue in material particular, the policy is voidable at the instance of the insurer. Sometimes the answers are made the "basis of contract". In such a case the policy is voidable if any of the statements, whether material or not, is untrue (l). All material facts within the knowledge of the assured must be disclosed by him to the insurer. He must not also be guilty of a material mis-statement.

Where the duty to disclose is defined in the contract, the special stipulations will govern the question. Generally the duty to disclose extends to "material facts". These include (a) facts which affect the nature or incidence of the risk and (b) the character of the assured. Materiality is a question of fact. The assured must disclose not only all material facts which he believes to be material but all facts which a reasonable man would regard as material (m).

Materiality is determined by the facts existing at the time the disclosure should have been made. Further, material facts must be truly disclosed; substantially inaccurate or misleading statements must amount to a breach, though unimportant mis-statements or omissions are disregarded (n).

Notice that non-disclosure of a material fact would avoid the contract. A mis-statement honestly made will not, unless it be one of the statements which is made the basis of the contract, otherwise fraud must be proved (o).

Duty of disclosure comes to an end when the contract is complete. Material facts which come to the knowledge of the assured subsequently need not be disclosed (p). The duty however continues during the pendency of the negotiations and if any material fact arises during the interval, the assured is bound to disclose the same, e.g. the fact that insurance has been refused by another company (q).

A policy sometimes contains an express provision that the assured warrants the accuracy of all statements made by him. Such a term creates a contractual liability as regards disclosure and if in such a case a statement is subsequently found false, the policy is avoided, irrespective of any question of materiality (r).

Question of Agent's knowledge

Before the knowledge of an agent can be imputed to the insurer, it must be established: (1) that he was in fact acting as the agent of the insurer in the transaction, (2) that it was his duty to obtain the knowledge in the course of his duties, and (3) to place the same at the disposal of his employees. Thus if the agent describes the premises inaccurately in case of fire insurance the underwriters are regarded as being aware of the misdescription (s). Disclosure to agent is disclosure to the principal. If however the agent and the assured collude to effect a fraud on the underwriters, the latter can repudiate the transaction, for the agent ceases to be an agent in such circumstances (t).

(k) See Pratt & Mulla's Stamp Act, p. 61 & Surajmall v. Triton Ins. Co., 52 Cal. 408.

(l) Dawson's Ltd. v. Bonnin (1922), A.C. 413.

(m) Joel v. Law Union etc. Ins. Co. (1908), 2 K.B. 863.

(n) Dawson's Ltd. v. Bonnin (supra).

(o) Newcastle Fire Ins. Co. v. Macmorran (1815), 3 Dow. 255; Anderson v. Fitzgerald

(1853), 4 H.L.C. 484.

(p) Cory v. Patton (1872), 7 Q.B. 304.

(q) Re Yajir & Guardian Ass. (1912), 108 L.T. 38.

(r) Newcastle Fire Ins. Co. v. Macmorran (supra).

(s) Pimme v. Lewis (1862), 2 F. & F. 778.

(t) Biggar v. Rock Life Ass. Co. (1902), 1 K.B. 516.

The duties of the insured and his agent as to disclosure were considered recently in by Desai J. in a Bombay case (u) as follows: (1) the assured must disclose to the insurer, before the contract is concluded, every material circumstance which in the ordinary course of business ought to be known to him. "Circumstance" in this connection includes any communication made to or received by the assured. Where the insurance is effected through an agent, the agent must disclose to the insurer (a) every material circumstance which is known to himself, an agent being deemed to know every circumstance which in the ordinary course of business ought to be known by or to have been communicated to him. (b) Every material circumstance which the assured is bound to disclose unless it comes to his knowledge too late to communicate to the agent. (2) The duty to disclose continues till the contract is concluded and a contract is deemed to be concluded when the proposal of the assured is accepted by the insurer whether a policy is then issued or not. (3) In the case of loss of subject-matter of insurance, an agent, whose duty it is to keep his principal informed is bound to send information of loss by telegram or telephone when it is practicable to do so. In every case, reasonable means of communication must be availed of, though it is not necessary that extraordinary steps should be taken or vigilance of extraordinary nature should be exercised. (4) Though the description of the subject-matter forms the basis of the contract of insurance, what is necessary is that such description should be adequate or it must substantially describe the property insured. The notice and extent of the interest of the assured in the subject-matter however cannot be called "description" of the goods.

Kinds of fire policies

Various kinds of such policies are known: (i) A "specific policy" means a policy in which the value insured against is specified.

(ii) "Average policy". This is a policy which covers more than one risk. The amount of loss in such a case has to be borne proportionately, i.e. not the whole loss is payable but such proportion thereof as the sum insured bears to the whole value of the policy.

(iii) "Floating policy", also called a 'floater'. It is a policy taken out on commodities which are frequently changing, e.g. goods in a warehouse.

(iv) "Valued policy", i.e. a policy where the value of the subject is specified in the policy.

Fire policies may also be (i) annual, (ii) short period, or (iii) long period policies.

Risk

A fire policy protects the assured against "fire". There is no "fire" unless there is ignition. Heating without ignition is not "fire". Lightning is not included nor electricity. Ignition must be of the property insured or the premises where it is situated. The cause of the "fire" is immaterial. It may be caused by the assured's own negligence (v). It might have been even deliberately caused, provided it is not the act of the assured himself. "Fire" does not include "explosion". If however the explosion is caused by "fire" or if explosion causes fire which causes the loss, the loss is covered (w).

Loss: Loss proximately caused by fire is recoverable. The subject-matter need not have been burnt. "Loss" includes loss which is the natural consequence of fire, e.g. falling of roof. It also includes "loss" which is the reasonable and probable result of fire, e.g. property destroyed by water used to extinguish the fire, property destroyed by fire-brigade to prevent fire from spreading (x). Theft during the fire is also covered (y).

(u) Vijay Kumar v. New Zealand Ins. Co. Ltd., 56 Bom. L.R. 341.

(v) Dixon v. Sadlar (1839), M. & W. 405; Harris v. Pollard (1941), 1 K.B. 462.

(w) Stanley v. Western Ins. Co. (1868), L.R. 3 Ex. 71.

(x) Stanley v. Western Ins. Co. (supra); Ahmedbhai v. Bom. Fire etc. Co., 29 T.I.R. 96.

(y) The Knights of St. Michiel (1898), p. 30.

Excepted perils

Fire policies generally exonerate the insurers from loss by fire caused during riots, civil commotion, explosion, military operations, etc. Where the cause of the loss is an excepted peril the assured cannot recover, e.g. an incendiary bomb causing an explosion which sets a warehouse on fire, where military operations are excepted (z).

Subject of insurance: The property intended to be covered must be properly described. If a "house" is insured against fire, it will not include household goods and things of special value. Property held in trust or as commission agent is also not covered. Loss of profits of a business conducted in such property is also not covered, unless specially provided for, nor loss of rent, subject to the same condition.

Though the description of the subject-matter forms the basis of the contract of insurance, what is necessary is that such description should be adequate or it must substantially describe the property insured. The nature and extent of the interest of the assured in the subject-matter, however, cannot be called "description" of the property.

Policy retrospective: It has been recently held by the Bombay High Court that with regard to fire insurance policy it is a question of intention in each case whether the policy was to have retrospective effect or not. It is not necessary that the words like "lost or not lost" should appear in the policy. Where therefore a cover note issued on 18th June assured the risk from 15th June and it appeared that, unknown to both parties, the goods had been destroyed by fire on the 16th June, held, the insurance company was liable and that no question of mistake under sec. 20 of the Contract Act arose (a).

Terms of policy

In order that a stipulation may amount to a condition the intention of the parties to make it so must plainly appear from the terms of the policy. An ambiguous stipulation will not be construed as a condition (b).

Clauses in fire policy: Some important cls. in a fire policy may be noted:

(i) **"Average clause":** Generally the actual loss caused by fire is recoverable, not loss proportioned to the value insured, as in marine insurance. This is countered by the above cl. It provides that if the insured thing is, at the time of loss, worth more than the amount insured by the policy, the assured "shall be his own insurer" for such excess, i.e. he shall bear such proportion of the loss as the sum insured bears to the total value of the policy.

(ii) **Contribution clause:** This is inserted when the subject is insured with more than one insurer. In such case, the assured cannot recover the full loss from any one of them but can only recover the same rateably from each.

(iii) **Marine clause:** When goods are insured both under marine and fire policies, the fire insurer inserts the cl. stipulating that he will be liable only for any excess over that covered by the marine policy.

(iv) **Alteration clause:** This cl. provides that the assurance will cease to attach if, without previous sanction of the insurers, the trade or manufacture carried on in the premises is changed, so as to increase the risk, or if the building insured becomes unoccupied or if the property assured is removed to a place other than that stated in the policy or if the interest of the assured passes from him otherwise than by will or operation of law.

(v) **Reinstatement clause:** This cl. gives the insurer option to restore the premises instead of paying the money to the assured. The insurer must make his election within a reasonable time. Once he elects to reinstate, he becomes bound to restore the property to original condition. He must also do so within a reasonable time.

(z) Rogers v. Whittaker (1917), 1 K.B. 942.

(b) Simmonds v. Cockill (1920), 1 K.B.

(a) Indian Trade & General, etc. v. Bhailal, 55 Bom. L.R. 874.

843.

(vi) **Salvage clause:** This permits the insurer to enter the premises immediately on receipt of notice of loss and take steps to mitigate the loss. Thereby the insurer does not admit his liability. He must not remain in possession of the property longer than necessary.

(vii) **Arbitration clause:** This cl. provides for arbitration in case of dispute. It is regarded as merely a condition and not as condition precedent to the filing of an action for claiming a loss. Sometimes it refers only to the question of loss (c).

Alteration of risk: The underwriters are only bound to indemnify against the particular risk insured. If the risk is altered their liability ceases. The alteration may be as regards the subject-matter or its locality or its circumstances. The alteration must be material, however; it must make the risk a different risk (d).

Making claim

The assured in order to claim the loss, must: (i) give notice in writing to the insurer of the loss, immediately after the occurrence. In the case of an agent, whose duty it is to keep his principal informed, he is bound to send information of loss by telegram or telephone when it is practicable to do so. In every case reasonable means of communication must be availed of, though it is not necessary that extraordinary steps should be taken or vigilance of extraordinary nature should be exercised. (ii) Within a certain time (generally 15 days) thereafter, he must submit to the insurer, a statement containing reasonable particulars of the loss and damage, with the estimated value of each article. (iii) He must produce proper evidence to support his claim, if the insurer so requires.

Generally the loss is estimated by "assessors". The assured, however, cannot recover the loss if (i) it is due to the wilful misconduct of himself or his agents; (ii) if it is due to the "inherent vice of the subject", unless the policy otherwise provides. Notice that an assured cannot recover anything more than the actual loss suffered by him, even under a valued policy. This is because a fire policy is a contract of indemnity only (e).

Salvage: Insurers are entitled to enter upon and remain on the property which is insured in case of fire. They are also entitled to take possession of the salvage there. The assured also on his part is bound to minimize the loss.

Assignment of policy

A fire policy being a contract to indemnify the assured only, cannot be assigned without the consent of the insurer. In India under sec. 135 of the Transfer of Property Act, a fire policy cannot be assigned without a transfer of the property insured to the assignee also. The assignment may be made by indorsement or other writing. The assignee of such policy in whom the property, the subject of insurance, is absolutely vested, has all the rights of suit as the original assured had, under the policy. Of course, he also takes it subject to all the equities attaching to the policy, in the hands of the transferor. Under sec. 49 of the above Act, a transferee for consideration of an immoveable property insured against fire, is entitled to call upon the transferor to apply any money received by him under a fire policy, to reinstate the property.

Subrogation

This is the right which the insurer gets to all the benefits which the assured had in respect of the thing insured on payment of the whole loss. The right arises only on payment of the whole loss. If the property is insured for less than its actual value, the insurer will not enjoy this right on payment of the policy amount. The rights of the assured, both in contract as well as tort, with regard to the subject, pass to the insurer under this rule. Thus if the loss is caused by the negligence of a party, the insurer,

(c) *Jurudini v. National, etc. Ins. Co. Ltd.* (1915), A.C. 499.

(d) *Law Guarantee, etc. Society v. Munich*

Re Insurance Co. (1912), 1 Ch. 138.

(e) *Castellain v. Prestno* (1883), 11 Q.B.D. 401.

under the above rule, becomes entitled to recover damages for the same, though of course, he can file such a suit, only in the name of the assured.

The insurer however can recover under this rule, only that which the assured could himself have recovered. Thus if the assured could not have recovered compensation against a third party (e.g. being his own wife, who sets fire to the house), the insurer also cannot recover anything (f). The assured, on full payment of the loss by the insurer, is bound in law to hand over to the insurer all moneys received by him from whatever source in respect of the loss. It does not matter that such payment has been voluntarily made (g). The assured must also not do anything which might prejudice the rights which the insurer obtains by subrogation as above, e.g. he must not release a claim which he may have against another in respect of the subject-matter of insurance (h).

LIFE INSURANCE

This is not a contract of indemnity. It is a "contract in which one party agrees to give a given sum upon the happening of a certain event, contingent upon the duration of human life, in consideration of the immediate payment of a smaller sum or certain equivalent periodical payments, by another" (Bunyon). The consideration is called "premium". It is payable either in one sum (single premium) or by successive periodical instalments, the first instalment being always payable in advance. In case of periodical payments, payment on or before the due date, is generally the condition precedent to the continuance of the policy.

Life assurance generally takes two forms: (i) whole life assurance and (ii) endowment assurance. In the first case, the sum insured is payable only at death, the payment of the premium being either during whole life or for a period as the parties may choose to arrange. In the second case, the sum insured is payable on reaching a specific age or on death before reaching such age (in which event, the amount becomes payable to the heirs of the person insured). This form is useful as an investment. Life assurance can be had on "with-profit basis" or on "non-profit basis". In India at present, life assurance business has been nationalised and is carried on exclusively by the Central Government controlled "Life Insurance Corp. of India" (see Act of 1956).

Insurable interest: This is an essential pre-requisite. It must be of a pecuniary character. Otherwise the policy will be void, as a gambling policy. The name of the person interested therefore must always be inserted in the policy. It is sufficient, however, that such interest exists at the date of the policy. It need not exist at the date of death (i).

The following have been held to have "insurable interest": (i) Oneself, in one's own life; (ii) wife and husband, in each other's life, (iii) a creditor, in the life of his debtor; (iv) a surety in that of his principal debtor; (v) joint promisors; (vi) trustee and executor; (vii) an employee on certain salary for a certain period in his master's life. A contingent interest can also be insured. Notice, however, that parents have no such interest in their children's life, nor have the children in their parents' lives, unless they are under a legal obligation to maintain and educate them (j).

Procedure: A local agent of the company generally acts in the matter. He is, however, an agent of the company only to receive proposals. He cannot bind the company by the policy. If, however, he is authorised by the company to accept proposals also, the company is bound by his acts. He cannot alter conditions fixed by the company. If the agent receives premium after notice of breach of a term in the policy, the company may be bound by his acts, e.g. assured going to a foreign country. An Insurance Agent does not cease to be so under sec. 44, because he has, with the consent of the principal,

(f) *Midland Ins. Co. v. Smith* (1881), 6 Q.B.D. 561.

(g) *Stearns v. Village Main Reef. Co.*, 21 T.L.R. 236.

(h) *West of England, etc. Co. v. Isaacs*

(1897), 1 Q.B. 226.

(i) *Dalby v. India, etc. Co.* (1855), 2 Sm. L.C. 241.

(j) *Howard v. Refuge Friendly Society* (1886), 54 L.T. 644.

done a small amount of outside business of a character not engaged in by his employer (j1).

Declaration

The company generally acts on a "proposal" or a "declaration" to be made by the person assured. This is a statement required to be made by the assured and signed by him, containing specified information or answering certain specified questions concerning the life insured and other matters connected with or more or less affecting the risk. Questions asked of the assured generally refer to (i) his age, (ii) health, (iii) habits of life, and (iv) previous history, and (v) particulars of his medical attendant. Statements made by such last persons on a reference to them by the company however do not bind the assured. Similarly, answers given to the medical examiner employed by the company, if inaccurate, do not invalidate the policy (k). The "proposal" generally states that the statements "are true and are taken as the basis of the contract". If these words are absent, the answers are mere "representations" and not "conditions". The effect of the above words is that the assured warrants the truth of the statements made. If anything therein is untrue, whether to his knowledge or not, and whether material or not, it will avoid the policy, e.g. if the answer says that the assured is not affected by a certain illness, when in fact he was affected by it, even for a short period; if the answer states that the assured is of temperate habits, when in fact he is not. If, however, the statement is prefaced by the words, "the assured believes" or "is not aware of", the warranty will only extend to belief. The "declaration" may also be so framed as to exclude liability for innocent mis-statement or non-disclosure. The declaration holds good till the completion of the contract. Any material change in the interval, e.g. illness, change of medical attendant, must be notified to the insurer, otherwise, the policy will be bad for breach of warranty of continued good health (l). Statements made to medical examiner are also mere representations, unless otherwise provided or unless made the basis of a policy. Statements made by the usual medical attendant of the assured, are not warranties. Similarly, statements made by referee are not warranties. The "declaration" is generally embodied in the policy, directly or by reference. Notice that life insurance being a contract "*uberrimae fidei*" not only fraud, but concealment or mis-representation of a material fact by the assured will avoid the policy, whether it is connected with the cause of death or not (m). The assured must disclose all material facts, whether asked or not. Materiality is a question of fact in each case (n). In case of life assurance policy it has been held that once the age given by the assured is admitted by the company, the latter is precluded from disputing the correctness of it unless the admission is procured by fraud. Where the age is not admitted, the burden of proving the age is initially on the person claiming under the assurance (o).

Premium

The assured becomes liable to pay the premium as soon as the contract of insurance is complete. Non-payment of premium however will not deprive the assured of the protection of the policy unless such payment is made a condition precedent to liability (p).

Risk: The risk generally commences on a binding contract being concluded, i.e. the issue of the policy. Payment of premium, however, may be made a condition precedent to the policy being operative. The premium is payable at intervals, generally annually and in advance.

"Death" may be from natural causes or accidentally. Even if death is caused by the criminal act of a third person, it would be covered. Death caused by the criminal act of the assured himself however, e.g. suicide, is not covered, nor is death caused by a capital sentence. Death caused by any excepted causes, e.g. military service, is also not

(j1) Sorabji v. Oriental Life Ass. Co., 48 Bom. L.R. 123 (P.C.).

(k) Joel v. Law Union & Crown Life Ins. Co. (1908), 2 K.B. 863.

(l) Sushila Devi v. Oriental Govt. L. Ins. Co. 1947(2), Mad. L.J. 227.

(m) London Ass. v. Mansel (1879), 11 Ch.

D. 363.

(n) Mutual Life Ins. Co. v. Ontario Metal Products Co. (1925), A.C. 344.

(o) Maneklal v. Yorkshire Ins. Co. Ltd., 41 Bom. L.R. 353.

(p) Addil & Sons v. Ins. Corp. (1898), 14 T.L.R. 544.

covered. Note that where suicide is an excepted cause, suicide even while insane, will fall within the exception, unless the assured at the time was unable to appreciate the nature of the act altogether (q). If assured was sane at the time, policy money will be irrecoverable, because law does not allow trading in a felony (r).

Kinds of life policies

Life policies are of various kinds: (i) "Whole life policy": In this, the sum fixed is payable on death alone. (ii) "Endowment policy": In which the sum fixed is payable on attaining a particular age or on death before that date. Two risks are insured in such a policy. The premium is therefore higher. The above two kinds of policies may be with or without the benefit of bonus, i.e. a share of profits distributed annually. (iii) Policy upon "joint lives", e.g. partners: In such a case, the company pays a stated sum for loss of partner's share in the partnership by death. The premium in such cases is generally paid out of the partnership assets. (iv) "Annuities": Under such a policy, the amount is not payable in lump on death but is payable yearly in smaller sums. (v) "Short-term policy" is for a shorter period than life. (vi) "Limited payment policy": In this, payment of premium ceases after a certain period. (vii) "Ascending scale policy": In this, the premium increases gradually. (viii) "Sinking fund policy": This is taken out by a company to pay off the debenture debts of the company. At the end of the period the fund is payable. (ix) "Indisputable policy": Under such a policy, the insurers are estopped from avoiding the policy on any ground except fraud. Under sec. 45 of the Insurance Act, 1938, no life policy can be called in question, after the lapse of two years, for mis-statement except on the ground of fraud.

Renewal: A policy can be renewed after its expiry or lapse, by mutual consent. A life assurance policy is a policy continuing till death. It can therefore be renewed at any time by performance of the renewal conditions. Sometimes days of grace are allowed. In fire policy 15 days are allowed. In life policy 30 days. A policy can therefore be renewed by payment of premium during this period. If loss occurs during this period, before payment of premium, the assured will be protected (s).

Surrender value: This means the value which a life assurance company assesses and is prepared to pay for the assured surrendering his interest under the policy. It is generally paid for policies on which three full premiums have been paid. As the duration of the payment increases, the surrender value also increases. It is generally calculated on the difference between the cost of a new policy and the value of the future premiums payable to keep alive the old policy.

Assignment: According to English Law an assignment of a life policy can be made by endorsement on the policy or by a separate instrument made according to a prescribed form. It must be followed by notice in writing to the insurer. The date of receipt of notice determines priority of all claims under the assignment, as between the insurer and the assignees. The insurer is bound to give written acknowledgment of receipt of notice. In India, the matter is now governed by sec. 38 of the Insurance Act, 1938. Under the sec., an assignment of a life policy can be made only by endorsement on the policy or by a separate instrument signed by the assignor and attested by one witness. Written notice of the assignment has to be given to the insurer, together with the endorsement or instrument itself or certified copy thereof. In absence of such notice, any dealing by the insurance company in respect of the claim will be valid. On such assignment and notice, the assignee is vested with all rights of suit with regard to the policy. It is a question of fact in each case whether a purported "assignment" really amounts to an "assignment" in law. A present assignment, however, followed by words of defeasance to be operative in certain contingencies does not make it ineffective (t).

Return of premium: If the policy is set aside on the ground of fraudulent misrepresentation by the assured, no premium will be returnable. If, however, the policy is sought to be avoided "*ab initio*", on ground other than fraud, e.g. negligent mis-

(q) Clift v. Schewabe (1846), 3 C.B. 437
Ex. Ch.

(r) Beresford v. Royal Ins. Co. (1938),
A.C. 586.

(s) Salvin v. James (1803), 6 East 571.

(t) Bai Laxmi v. Jaswantlal, 49 Bom. L.R.
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statement, which is made the basis of contract, the premium paid can be recovered. The policy may however contain a clause that the premium will be forfeited if the policy becomes void. Such a term is held to be valid (u). In such a case, no premium can be recovered. If the policy is illegal, e.g. because there is no insurable interest, premiums cannot be generally recovered back (v).

Making claim: Death must be proved by production of a death certificate and a declaration of the identity of the person described in such certificate. The claimant must also establish his title to receive the moneys, by producing proper representation to the deceased. Notice that in no case, can an assured recover under a policy, anything more than the value of the insurable interest at the date of the policy. Under sec. 39 of the Insurance Act, 1938, the insurer, at the time he effects a policy, may nominate a person or persons to whom the moneys are to be paid. Such nomination can be made in the policy itself or by endorsement on the policy or by a separate instrument or by will.

The Insurance Act: The Insurance Act of 1938 (India) is a comprehensive piece of legislation intended to place under Government control, as far as possible, the business of insurance, in all its aspects, as carried on in India. It covers life, fire and marine insurance as well as provident and other kinds of insurance business. The following are some of its more important provisions: (i) All persons, whether corporate or not, carrying on business of insurance of any kind, in India (including British and other foreign companies carrying on such business in India through agents or otherwise), must obtain a certificate of registration from the Controller of Insurance before they can carry on their business (sec. 3). The Controller is given power to withhold or cancel such certificate, in case of foreign companies, if their respective States debar Indians from carrying on insurance business within their territories. (ii) In case of Life Companies, a minimum of Rs. 50,000, is made compulsory as working capital. (iii) Further, certain amount of compulsory deposit is required in each type of insurance business, e.g. life insurance only, Rs. 2,00,000; fire insurance only, Rs. 1,50,000, marine insurance only Rs. 1,50,000; accident and miscellaneous insurance (including workmen's compensation) only, Rs. 1,50,000. When these businesses are combined, the deposit to be made is higher, e.g. Rs. 3,00,000 if life and any one of the above three are combined. These deposits (to be made with the Reserve Bank of India) are not liable to attachment and also cannot be assigned or charged by the insurer. Further, they can be applied only towards discharge of liabilities arising from the particular kind of insurance for which they have been respectively made and towards no other (sec. 7). (iv) Separate accounts of each of the various kinds of insurance business have to be maintained. Excess of receipts over expenditure in case of life insurance, shall form a separate fund, which shall stand as absolute security of the life policyholders (sec. 10); (v) Balance sheet, profit and loss account and profit and loss appropriation account shall be prepared and audited annually as laid down in the Indian Companies Act. (vi) Actuarial report of life insurance business transacted shall be made once every five years. The abstract of the report shall be certified by the principal officer of the insurer (sec. 13). (vii) Assets equal to 25 per cent of the amount of liability to life policyholders are required to be invested in government securities and 25 p.c. of the same in approved securities and the balance in certain approved investments (sec. 27). (viii) Loans to directors, managing agents, managers, secretary or any other officer of the company are prohibited, except loans against life policies within their surrender value (sec. 29). (ix) No managing agent can be employed by insurance companies (sec. 32). (x) No person can act as an insurance agent unless he is duly licensed. No company can pay to such agent, by way of commission, more than 40 p.c. of the first year's premium payable on policies effected through him and 5 p.c. of the renewal premium (in case of life insurance) and in other cases, more than 15 p.c. of the premium (sec. 40). (xi) No rebate can be allowed or received on premium or commission, except such rebate as is allowed in the published prospectus or tables of the insurer (sec. 41). (xii) Renewal commission payable to an insurance agent, cannot be stopped by the insurer, except in case of fraud, provided such agent has acted for him for not less than 10 years (sec. 44). (xiii) In case of insurance companies incorporated under the Indian Companies Act, not less than $\frac{1}{4}$ th of

(u) *Sparenberg v. Edinburgh Life Ass. Co.* (1912), 1 K.B. 195.

(v) *Harse v. Pearl Life Ass. Co.* (1904), K.B. 558.

the total number of directors shall be directors elected by the policyholders as prescribed by the Rules (sec. 48). (xiv) No bonuses can be paid except out of surplus profits as made out by actuarial reports (sec. 49). (xv) All insurance business, on the "dividing principle" under which the assured gets not a fixed sum but a certain percentage of the total collections from other assured, is prohibited (sec. 52). (xvi) No insurance company can be wound up voluntarily except for purposes of amalgamation and reconstruction. The grounds of winding up insurance companies by the Court are also enlarged. They include (i) failure to make or maintain the statutory deposits; (ii) failure to observe the requirements of the Act; (iii) if the returns or the report of investigation of the Controller of Insurance shows that the company is insolvent; (iv) if the continuance of the company is prejudicial to the interests of the policyholders. In the above cases, the application has to be made by the Superintendent. (v) An insurance company can also be wound up by Court on a petition of 1/10th of the total number of shareholders, holding 1/10th of the whole share capital or on the petition of 50 policyholders holding policies of the total value of Rs. 50,000 which have been in force for 3 years (secs. 53-54).

Under secs. 52A-52G, the Central Government has got power to appoint an Administrator to manage the affairs of an Insurance Co., if it is satisfied, on the report of the Controller, that the insurer is acting in a manner prejudicial to the interests of the policyholders. Wide powers are given to such Administrator. The amendments of 1955 give power to the Administrator to take out misfeasance proceedings against persons connected with the management of such Co. (s. 106) and also a power to attach, before full investigation, any property in possession of such persons, which he has reason to believe, belongs to the insurance Co. (s. 52 B.B.).

CHAPTER XV

INCORPORATED COMPANIES

Historical Retrospect: The Companies Act of 1913 was defective in many important particulars. It was also found to be unsuitable for the changed conditions, brought about by World War II. A complete overhaul of the Act was therefore necessary. The Companies Act of 1956 (Act I of 1956), was thus passed. It now makes Company Law up-to-date and most comprehensive. It came into operation on 1st April 1956.

Important changes made by the New Act

(1) The words "private limited" are now required to be added in the name cl. of the Memo. in case of private Limited Co.s (s. 13). Further, the Central Government is now given the power to compel a Co. to change its name. Certain articles which were found in Table A of the Act of 1913, and which were made compulsorily applicable to Co.s are now embodied in the secs. of the new Act. (2) All investments must now be made and held by the Co. in its own name (s. 49). (3) The contents of the Prospectus are enlarged (s. 56). Minimum subscription is now statutised (s. 55) and 120 days only, are allowed for its collection (s. 69). Provision is made where shares are to be quoted on the Stock Exchange (s. 73). (4) Only two types of shares can be issued now: (i) Preference and (ii) Equity (s. 85); deferred shares are abolished. Issuc of shares at more than 10 per cent discount is prohibited (s. 79). Premium received on issue of shares must now be transferred to a separate account called "share premium account" (s. 78). Disproportionate voting rights on shares are abolished (s. 88). Right of appeal to Central Government is now given where directors refuse to register a transfer (s. 111). Debenture holders cannot now have voting rights (s. 117). (5) All Co. meetings now require 21 days notice (s. 171). Notice must be accompanied by explanatory statement (s. 173). Members can now circulate their resolutions before the meeting (s. 188). Extraordinary resolution is abolished and a new type of resolution "requiring special notice" is introduced (s. 199). (6) Remuneration payable to Managing Agents, Managing Directors, Secretaries and Treasurers and managerial personnel generally, is now statutised at 11 p.c. of net profits of the Co. (s. 198). This is one of the most

important changes. Appointment of "associates" and "relatives" of directors, managing agents and others on the staff of a Co. is now strictly regulated (s. 314). One person cannot hold more than 20 directorships (s. 275). Superannuation bar for directors at 65 years age is introduced (s. 280). A clear division of powers is now made between directors, managing agents and shareholders. Loans to directors of sister Co.s is now controlled (s. 295). (7) Central Government can now by Notification abolish Managing Agency system altogether (s. 324). Even otherwise, all managing agencies will end automatically by 15th December 1960 (s. 330). Managing Agents cannot now be appointed for more than 15 years for the first time and 10 years for other times (s. 328). Any variation in the terms of their employment now requires Central Government's sanction. Their maximum remuneration cannot be more than 10 p.c. of net profits (s. 348). Loans to Co.s under common management are now controlled (s. 370). Managing Agents cannot appoint more than 2 *ex-officio* directors (s. 377). (8) Shareholders can now apply to Court in cases of oppression and mismanagement (s. 397).

Company and Partnership distinguished: A Co., i.e. an incorporated Co. is something much more than and is totally different from a partnership as constituted under the Partnership Act. (i) A Co. formed under the Indian Companies Act is a distinct legal entity having a separate existence of its own as distinct from the members constituting it. A partnership, commonly called a "firm" has no separate legal existence apart from its members. A Co. on incorporation attains the status of an artificial person, with a perpetual succession and a common seal, which a partnership does not. In the leading case of *Saloman v. Saloman & Co. Ltd.* (a) S had sold his boot business to a Co. composed of himself, his wife, daughter and four sons, each of whom had only one share in the company, S holding the remainder. The sale price was £30,000, which was paid to S by giving him 20,000 fully paid up shares of £1 each and £10,000 in debentures. The Co. was subsequently wound up. In a contest between S as the debenture-holder and the unsecured creditors of the Co. the latter contended that the Co. was really the same person as S and he could not owe money to himself. Vaughan Williams J., in the first court held that the Co. was a mere agent for S and that S therefore was bound to indemnify the Co. (his agent) for losses (i.e. the unsecured debts) sustained by it. It was held by the House of Lords, however, that the Co. at law was an altogether different person from the persons signing the Memo. of the Co.; that the Co. was not an agent for S and that as debenture-holder, S was entitled to priority over the unsecured creditors of the Co. in respect of the balance of the purchase money due to him. (ii) A partnership in business for the purpose of gain, of more than 20 persons is illegal (s. 11). A Co. may consist of any number of persons (not less than two). (iii) A partner cannot transfer his share without the consent of the other partners, whereas the essence of the conception of a Co. is the transferability of its share capital. (iv) Unless otherwise provided by the partnership agreement, a partnership is dissolved by the death of a partner. The death of a shareholder has not the effect of dissolving a Co. (v) Each partner is an agent of the firm to make contracts. A shareholder is not an agent for the Co. (vi) The property of a "Co." belongs to the legal "persona" called the "Co." and not to the shareholders as such. In case of partnerships, it belongs to the partners collectively. (vii) A partner is liable for the debts of the partnership, both to the extent of his interest in the partnership assets as also individually, i.e. his private property too is liable, in other words his liability is unlimited. The liability of the shareholder of a limited liability Co., however, is restricted to the amount due and unpaid on the shares held by him and to the extent of his guarantee, if the company is limited by guarantee. A shareholder in these cases cannot be held liable for all the debts of the Co. whatever their extent may be. (viii) All partners are entitled to take part in the management of the partnership business. Shareholders have only very restricted rights to interfere in the management of the affairs of a Co., which is in the hands of the directors. (ix) There are certain disabilities imposed by law on limited Co. which do not obtain in case of private partnership, e.g. a Co. cannot buy its own shares, it cannot alter its share capital except under certain conditions. The partners in a partnership firm, however, can by mutual consent vary the terms of partnership and can also buy up the share of any partner.

How a Company can be Incorporated: Co.s may be incorporated in a variety of ways. Thus: (i) a Co. may be incorporated by being formed and registered under the present Act in the manner provided by the Act. It may also have been formed and registered under any of the earlier Companies Acts of 1857 or 1860, or 1866 or 1882, or 1913 (s. 3). (ii) A Co. may also be incorporated by Royal Charter or Letters Patent, e.g. the Bank of England or the East India Company. The special features of such Co.s are that (a) their members are not personally liable for the debts of the corporation, (b) the debts also, are extinguished on dissolution, and (c) the corporation can exercise all powers of an ordinary individual as regards dealing with property, entering into contracts, etc. although the charter gives only restricted powers.

(iii) A Co. may also be incorporated by means of a special Act of the Legislature, either of the British or other Parliament or of the Government of India. Such Co.s are called "Statutory Companies", e.g. the London and North Western Railway Company. These Co.s are generally formed to carry out some special public undertaking, e.g., Railway, Waterworks, Gas, Tramways, etc. The carrying out of such undertakings usually involves committing acts, which would amount to nuisance at common law. The Acts incorporating such Co.s, therefore, grant them power and permission to do such acts. In other respects, such Co.s are similar to ordinary limited Co.s incorporated under the Companies Act; the liability of their members is limited by shares, their powers are limited by the provisions of the Act and they cannot use their funds for other purposes, however beneficial they may be. Instances of Statutory Co.s in India are the Imperial Bank of India, the Reserve Bank of India, etc. Notice that certain class of incorporated Co.s have special Acts, which govern them, e.g. Co.s which are governed by Insurance Act 4 of 1938, Provident Insurance Societies which are governed by Act 5 of 1912 and Co-operative Societies which are governed by Act 2 of 1912 and Registered Societies which are governed by Act 21 of 1860 and Banking Companies are governed by Act 10 of 1949.

Varieties of Companies: (i) Co.s may be, either (i) *public*, or (ii) *private*. A public incorporated Co. means a Co. which offers its share capital to the public generally for subscription. A private incorporated Co. is a Co. which, speaking generally, does not so offer its share capital to the public for subscription. Co.s may also be either (i) Co.s with limited liability or (ii) Co.s without limited liability. These last are called "*unlimited companies*". Limited Co.s comprise two classes: (a) *companies limited by shares*, i.e. Co.s having the liability of their members limited by the memo., to the amount, if any, unpaid on the shares respectively held by them, or (b) *companies limited by guarantee*, i.e. Co.s having the liability of their members limited by the memo. to such amount as the members may respectively thereby undertake to contribute to the assets of the Co., in the event of its being wound up. Of these two, the former is by far the most common. "Guarantee companies", on the other hand, are rarely found in the East, their most favourite place being America. This form is convenient for clubs, syndicates and other associations which do not require the interest of their members to be expressed in terms of cash. The whole property of such Co.s belongs to all the members in certain proportions.

(ii) **Joint-Stock Companies:** These have been defined as "associations of persons, incorporated to promote, by joint contribution to a common stock the carrying on of some commercial enterprise." These were originally partnerships, consisting of large fluctuating bodies of individuals, the shares of partners being transferable. They were unregistered and a limitation on the liability of their members was sought to be introduced into them. Such Co.s were common in the 17th and 18th centuries in England. Their chief difficulty was that persons dealing with them did not know whom to sue for their claims. The law, therefore, did not look upon them with favour. They were, however, made compulsorily registrable in England by the Companies Act of 1844. The principle of limited liability was only introduced for the first time by the Companies Act of 1862. In the present Indian Companies Act provision is made for the registration of such companies in Part IX. S. 566 defines such Co.s as follows:—"A 'Joint-Stock Company' means a company having a permanent paid up or nominal share capital of a fixed amount divided into shares of fixed amounts or held and transferable as stock (or divided and held, partly in one and partly in the other way) and formed on the principle of having for its members the holders of such shares and/or stock and no others."

(iii) "*One Man Companies*": These are Co.s in which one man holds practically the whole of the share capital of the company, while the remainder is held either by his relations or nominees. Being the largest holder, such a person is generally the sole or the managing director and enjoys full control over the company. Such Co.s are generally private Co.s, and often consist of either man and wife or of man, wife and children. *Saloman's Case* (supra) is an instance of one of such Co.s. Such Co.s, however, are not illegal. It should not be thought, however, that frauds would be allowed to be perpetrated under the guise of "one man companies". If a business is insolvent when sold to a "one man company", the Court has sufficient power under the Companies Act, to hold the directors guilty of fraudulent trading and as such, individually liable for all the debts of the Co. (see s. 542).

(iv) *Associations not for profit*: These are Co.s which do business and realise profit but do not divide it amongst its members. Their object is generally to promote commerce, arts, science, etc. Their management rests, not with a board of directors, but with a committee of management. Their membership is by election or on payment of a subscription. Such Co.s can be formed with limited liability under s. 25 of the Act, after obtaining a licence from the Central Government. They enjoy special privileges, one of them being that they need not use the word "Limited" as part of their names, as other limited liability companies have to do (see post). The powers given by the sec. have proved very useful and many kinds of associations have availed themselves of these powers in England, e.g. Medical Institutes, Law Societies, Chambers of Commerce, Clubs, Schools and learned Societies. The principle of limited liability generally takes the form of guarantee Co., in case of such associations.

(v) *Banking Companies*: These are defined as "companies which carry on as their principal business, the accepting of deposits of money on current account or otherwise, subject to withdrawal by cheque, draft or order". These Co.s are now governed by the Banking Companies Act (10 of 1949).

(vi) *Investment Companies*: These are Co.s whose principal business is the acquisition and holding of shares, stocks, debentures, or other securities, of other companies on behalf of and for the benefit of their members. They are governed by the same rules as other incorporated Co.s.

(vii) *Subsidiary and Holding Companies* (see post): For *Statutory Companies*, etc. see ante.

(viii) *Unregistered Company*: This has been defined by s. 582 of the Act, as any partnership, association or Co., consisting of more than seven members, which is not registered either under the Indian Companies Act of 1866 or under any Act repealed thereby, or under the Indian Companies Act of 1882 (not being a Co. whose registered office was in Burma, Aden or Pakistan immediately before the separation of that country from India or in Jammu and Kashmir immediately before 26 Jan. 1950) or under the present Act but not including a railway company incorporated by an Act of Parliament or other Indian Law or any Act of Parliament of the United Kingdom. Provision for the winding up of such companies has been made by ss. 582-590 of the Act.

(ix) *Foreign Company*: means a Co. incorporated outside India and having at the commencement of this Act a place of business in British India or which, thereafter establishes such a place of business in British India. Provision for such Co.s has been made in ss. 591-608 of the Act.

(x) *Unincorporated Companies*: These were large partnerships. Their shares were transferable. Their management rested with a select body of managers or directors. They were generally accompanied by a deed of settlement. Their continuity was preserved notwithstanding bankruptcy or death of their members. They were very common in the 17th and 18th centuries. Now they are extinct by reason of the provisions of the English and Indian Companies Acts regarding compulsory registration.

(xi) *Registered Societies*: These are not incorporated Co.s under the Companies Act. They are governed by a special Act, viz. Societies Registration Act (21 of 1860). Societies formed for the purpose of promoting science, art, literature, political education or charity, can obtain certain advantages by getting themselves registered under that Act. The Act lays down certain rules for the formation, registration and regulation of such societies.

Importance of Limited Companies: The importance of the institution of limited liability companies cannot be under-estimated. As Jessel M.R. said in *Jenkin v. Pharmaceutical Society*, "Limited Companies are offsprings of a proved necessity, that is that men should be entitled to engage in commercial pursuits without necessarily involving the whole of their fortune in that particular pursuit in which they are engaged." "The dominant and cardinal principle of these (Companies) Acts is that the investor shall purchase immunity from liability beyond a certain limit, on the terms that there shall be and remain a liability up to that limit" (b). The results of this new institution have not taken long to make themselves felt. As Buckley puts it (c) "the statutes relating to limited liability have probably done more than any legislation of the last fifty years to further the commercial prosperity of the country. They have, to the advantage, as well of the investor as of the public, allowed and encouraged the aggregation of small or comparatively small sums into great capitals, which have been employed in undertakings of great public utility, largely increasing the wealth of the country."

Companies to which the Act applies (s. 3): The Act applies to the following companies only: (i) Co.s formed and registered under the Act, i.e. (a) Co.s limited by shares; (b) Co.s limited by guarantee; (c) Co.s with unlimited liability; (d) private Co.s. (ii) Other "existing companies", i.e. Co.s formed and registered under Companies Act of 1866 or any Act or Acts repealed thereby and under the Indian Companies Act of 1882 or 1913; (iii) Co.s formed and registered under the Registration of Transferred Companies Ordinance, 1942 (54 of 1942) and to Co.s formed and registered in the merged territories or in Part B States under corresponding Acts or Ordinances in force therein before the extension of the Companies Act of 1913 thereto.

The Act does not by itself apply to: (i) Co.s registered but not formed under previous Companies Acts. They can however be registered under the present Act in the manner and subject to the conditions laid down in ss. 565-571. (ii) Unregistered Co.s. They can however be wound up under ss. 582-590 of the Act. (iii) Co.s incorporated outside India. If they establish places of business in India, however, they have to observe the provisions of ss. 591-608. The Act does not also apply to (iv) to Statutory Co.s and Co.s formed under Letters Patent or Royal Charter.

Definitions (s. 2): "*Articles*" means articles of association of a Co. as originally framed or as altered from time to time in pursuance of any previous Co.'s Law or of the present Act, including so far as they apply to the Co., the regulations contained, as the case may be, in Table B in the Schedule of the Companies Act of 1853, Table A in the first Schedule of the Companies Act of 1882 or in Table A in the first schedule of the Companies Act of 1913 or in Table A in Schedule I annexed to the present Act.

"Associate". This is one of the most important definitions, newly introduced by the present Act. The Act makes provisions for regulating the duties and obligations of what are called "associates" of (i) "Managing Agents" and (ii) of "Secretaries and Treasurers"; (for these provisions, see seq.). These "associates" may be of four types. They may be (i) an individual, (ii) a firm, (iii) a body corporate, or (iv) a private Co. Each of these types are separately and minutely described and defined by cl. 3 of s. 3. Under this clause an "associate" in relation to a Managing Agent means any of the following and no others:

(a) *Where the Managing Agent is an individual*—(i) any partner of his, (ii) any firm in which such individual, his "relative" or partner is a partner and (iii) any private Co., in which such individual, partner, "relative" or firm is, managing agent, or Secretaries and Treasurers or a director or manager, (iv) any body corporate, at the general meeting of which, not less than one-third of the voting power is exercisable or controllable by such individual or partner or partners, "relative" or "relatives", firm or firms and private Co. or Co.s.

(b) *Where the Managing Agent is a firm*—(i) any member of such firm, (ii) any partner or "relative" of such member, (iii) any other firm in which such member, partner or "relative" is partner, (iv) any private Co. of which the first-mentioned firm or any such member, partner, relative or other firm is, managing agent, Secretaries and

(b) *Ooregum Gold Mining Co. v. Roper*
(1892) A.C. 125, 145.

(c) *Re London and Globe Finance Corp.*
(1903), 1 Ch. 728.

Treasurers, director or manager, (v) any body corporate, at the general meeting of which, not less than one-third of the voting power is exercisable or controllable by the first-mentioned firm, or any such member or members, partner or partners, "relative" or "relatives", or other firm or firms.

This elaborate definition of an "associate" is intended to prevent the provisions of the Act relating to managing agents being evaded. Various devices were being employed by Managing Agents and Secretaries and Treasurers to get out of the stringent restrictions placed by the Act on their powers, rights and emoluments, by passing the benefit of these to their friends, associates and nominees. These devices are sought to be circumvented by the present Act, by extending the operation of the said restrictive provisions to the "associate" of managing agents, as also to the "associate" of the "Secretaries and Treasurers" of an incorporated Co.

To illustrate the meaning and implications of the above definitions the following example may be taken: A is Managing Agent of B & Co.; then, if A has partners, all such partners, if A is a partner in a firm called C & Co. all partners of C & Co., will be "associates" of Managing Agent A: Further, if A or any partners of A, or any member of C & Co. is managing agent, Secretaries and Treasurers, director or manager of a private Co., such private Co. will also be deemed to be "Associate" of the Managing Agent; still further, if A, his partner or partners or the firm or firms in which A is a partner, or partners, or the firm or firms in which A is a partner, control one-third of the voting power in another company (by holding shares therein or otherwise), such Company also will be regarded as "associate" of the Managing Agent A. Finally a "relative" of A and the others will also be regarded as an "associate". "Relative" is defined later.

(c) *Where the Managing Agent is a corporate body.*—(i) Any subsidiary or holding Co. thereof, (ii) the managing agent, (iii) the Secretaries and Treasurers, (iv) any Director, (v) Manager or (vi) officer of such body corporate, or of any subsidiary or holding Co. thereof, (vii) any partner or relative of such director, managing agent or manager, any firm in which such director, managing agent, manager, partner or relative is a partner and (viii) any other body corporate, at the general meeting of which not less than one-third of the voting power is exercisable or controllable by, the body corporate itself and the companies and other persons mentioned in (i-vii) hereof.

(d) *Where the Managing Agent is a private Co. or a body corporate having not more than 50 members,* in addition to persons mentioned in clause (c) (i-vii) above, (viii) any member of such Co. or body corporate.

Notice that where a person is an "associate" of another, within the meaning assigned to that word by the above definition, the latter will also be deemed to be an "associate" of the former.

"Associate" in relation to "Secretaries and Treasurers" means any of the following and no others: (a) Where Secretaries and Treasurers are a firm—same as in (b) above. (b) Where Secretaries and Treasurers are a corporate body—same as in (c) above. (c) Where Secretaries and Treasurers are private Co.—same as in (d) above. Notice that in case of Secretaries and Treasurers also, where a person is an associate in relation to another as defined by this cl., that other shall also be deemed to be an "associate" of the former.

"Body Corporate" or "corporation" includes a Co. incorporated outside India (i.e. a foreign Co.), but does not include a corporation sole.

Debenture: Includes debenture stock, bonds and any other securities of a Company, whether constituting a charge on the Co.'s assets or not; for debentures see *seq.*

"Director" includes any person occupying the position of a director, by whatever name called. The definition includes *de facto* directors. They are liable for any act of commission or omission in the same manner and to the same extent as *de jure* directors (d).

"Government Co." means a Co. in which not less than 51 per cent of the share capital is held by the Central Government or any State or States Governments or partly

by one and partly by the other (see s. 617). Special powers of audit regarding such Co.s are reserved to Government by the Act. Government is also given power to modify application of the Act to such Co.s under certain conditions (see ss. 617-620). Such Co.s cannot appoint Managing Agents (s. 618).

"*Issued Generally*" means, in case of a prospectus, issued to persons irrespective of their being existing members or debenture-holders of the body corporate to which the prospectus relates.

"*Manager*" means an individual (not being the managing agent) who, subject to the superintendence, control and direction of the Board of Directors, has the management of the whole or substantially the whole of the affairs of a company and includes a director or any other person occupying the position of a manager, by whatever name called and whether under a contract of service or not. *De facto* managers are therefore included and so also a director who actually manages the affairs of the company, besides being a director.

"*Managing Agent*" means any individual, firm or body corporate, entitled, subject to the provisions of the Act, to the management of the whole or substantially the whole, of the affairs of a company, by virtue of an agreement with the company or by virtue of its memorandum or articles of association, and includes any individual, firm or body corporate occupying the position of a managing agent, by whatever name called.

A "*Managing Agent*" is distinguished from a "*manager*" in that a "*manager*" is a person who manages the affairs of a company under the directions of the directors. He is thus under the full control of the directors. A "*managing agent*" on the other hand, is a person (firm or company), which is entitled to the management of the affairs of a company, under the control of the directors, *except* so far as is otherwise provided by the agreement appointing him or them, or by the Memorandum or the Articles. A Managing Agent, therefore, can have powers and privileges, which are not under the control of the directors, provided (i) they are granted by the agreement, Memo. or articles appointing him; and (ii) provided they are not inconsistent with the provisions of the Act relating to managing agents. Managing agency agreements frequently transfer to the managing agents, various powers which are really exercisable by the directors themselves or by the company, e.g. power of appointing *ex-officio* directors, powers of management, etc. This is now valid only so far as it is permitted by the Act.

"*Managing Director*" means a director who, by virtue of an agreement with the company or of a resolution passed by the company in general meeting or by its Board of Directors, or by virtue of its Memo. or Articles, is entrusted with any powers of management which would not be otherwise exercisable by him and includes a director occupying the position of a managing director, by whatever name called.

"*Member*" in relation to a Co. does not include a bearer of share warrant issued by the Co.

"*Memorandum*" means the Memo. of Asso. of a Co. as originally framed, or as altered from time to time in pursuance of the provisions of any previous Companies Law or of this Act.

"*Officer*" includes any director, managing agent, secretaries and treasurers, manager or secretary, and where the managing agent or secretaries and treasurers are a firm, also includes any partner thereof and where they are a body corporate, any director, managing agent, secretaries and treasurers or manager of the body corporate but, save in s. 477 (power to summon persons suspected to be in possession of Co.'s property), s. 478 (Public Examination of promoters, directors, etc.), s. 539 (penalty for fabrication of books), s. 543 (power of Court to assess damages against delinquent directors, etc.), s. 545 (prosecution of delinquent directors, members, etc.), ss. 621, 625 (Offences under the Act) and s. 633 (power to grant relief), *does not include an auditor*. This definition is important, because it defines who is an "*officer*" of a Co. Various secs. of the lay down penalties in the shape of fines and imprisonment for non-observance by "*officers*" of the Co., of the requirements of the Act. Notice that auditors are "*officers*" of a Co. except for the purposes of the secs. mentioned above.

"*Prospectus*" means any prospectus, notice, circular, advertisement or other document, inviting offers from the public for the subscription or purchase of any shares.

debentures of a body corporate. The word thus includes both subscription and sale prospectuses. Apparently, a newspaper advertisement of a prospectus would fall under this definition. The exemption under the old Act as regards newspaper advertisements which state that a proper prospectus has been filed with the Registrar, is deleted and is therefore no longer operative.

"Share" means share in the capital of a Co. and includes stock, except where a distinction between stock and shares is expressed or implied.

"Total Voting Power": In case of a body corporate means the total number of votes which may be cast in regard to that matter on a poll at a meeting of such body, if all the members thereof and all other persons, if any, having a right to vote on that matter are present at the meeting and cast their votes.

"Trading Corporation" means a "trading corporation" within the meaning of entries 43 and 44 in List I of Schedule VII of the Constitution Act. Under the above definition corporations owned or controlled by Federated States and carrying on business within such States only, are excluded, so also are Co-operative Societies.

"Recognised Stock Exchange": For the purposes of the Act, means a Stock Exchange, whether within or without India, which is notified by the Central Government as such in the Official Gazette for the purposes of the Act or any of its provisions.

"Secretaries and Treasurers" means any firm or body corporate (not being managing agent), which, subject to the superintendence, control or direction of the Board of Directors has the management of the whole or substantially the whole affairs of the Co. and includes any firm or body corporate, occupying the above position, by whatever nature called and whether under contract of service or not.

Managing agents often worked under the pseudo names of "secretaries and treasurers". Hence the present definition and inclusion of "Secretaries and Treasurers" in the definition of "associate" (see *ante*).

"Secretary" means any person appointed to perform duties which may be performed by a secretary under the Act.

Company defined (Ss. 3-7): Under s. 3 "unless the context otherwise requires": (i) "Company" means a company formed and registered under the present Act or an "existing company". (ii) "Existing Co." means a company formed and registered under: (a) any Act relating to Companies in force prior to 1866, which is repealed by Act 10 of 1866, (b) under Act 10 of 1866 or (c) Act 6 of 1882, or (d) Act 7 of 1913 or (e) under the Registration of Transferred Companies Ordinance, 1913, (f) under any corresponding Acts or Ordinance in force in the merged territories or in Part B States or in any parts thereof before extension thereto of Act 7 of 1913. (iii) "Private Company" means a company which by its article (1) restricts the right to transfer its shares (if any); (2) limits the number of its members to 50 (excluding persons in its employment and persons who were members while in its employment and who have continued to be members, though their employment has ceased and (3) prohibits any invitation the public to subscribe for any shares or debentures of the Co. Where two or more persons hold shares jointly, they shall be treated as a single member for the purposes of the above definition. Notice that employees and ex-employees, holding shares of the Co. as such, are not to be considered in arriving at the number of 50 under the present Act. Notice also that a private Co. need not now have any share capital, it may be a guarantee Co. (iv) "Public Company" means a Co. which is not a private Co.

Holding Company and "Subsidiary" (s. 4): For the purpose of the Act a company shall be deemed to be a "subsidiary" of another if and only if: (i) that other, "controls the composition of the board of directors" of the former or (ii) if that other holds more than half of the nominal value of the former's "equity capital" or (iii) if the first mentioned company is a subsidiary of a subsidiary of that other.

"Controlling the Composition of the Board of Directors" means that the "holding company", by some power exercisable by it, at its absolute discretion, without the consent or concurrence of any other person, has the right to appoint or remove all or the majority of directors of the subsidiary Co. Such power of appointment shall be deemed to exist if (a) a person cannot be appointed director in the subsidiary Co. without the holding Co. exercising the power of appointment in his favour, (b) if the appointment of a

person as director of the subsidiary Co. necessarily follows from his appointment as director, managing agent, secretaries and treasurers or manager of the holding Co. or from his appointment as to any other office or employment in the holding Co. or (c) if the directorship in the subsidiary Co. is held by the holding Co. itself or its subsidiary.

Notice the following points as regards the question, "whether one Co. holds more than half of the equity capital of another" and/or "whether it has the power to control the appointment of all or a majority of the directors of the other": (i) shares held or power of appointment held by the first Co. in a fiduciary capacity, as a trustee for another, shall not be taken into account; (ii) shares held or power of appointment held by the first Co., by virtue of the terms of any debentures or debenture trust deed, shall not be taken into account; (iii) shares held or power of appointment held by the first Co. or its nominee or subsidiary, as security only, for moneys advanced by the first Co. to the other, in the ordinary course of its business (provided lending of money is included in the ordinary business of that Co.), shall not be taken into account; (iv) except as otherwise provided in (i), (ii) and (iii) above, shares held or power of appointment exercisable by a nominee of the first Co., or by a subsidiary of the first Co. or by a nominee of such subsidiary (not being concerned in a fiduciary capacity), shall be treated as "held and exercisable by the first Co."

The test laid down by the Act for determining whether a Co. is "subsidiary" of another, is whether the second Co. has got a controlling power over the first. Such controlling power can be exercised in either of two ways: (i) by holding the whole or majority of the first Co.'s "equity capital" or (ii) by having the power to appoint the majority of directors of the first Co. The sec. goes into details as to when a company can be and cannot be said to have such controlling power. A subsidiary includes a sub-subsidiary. This is explained by the illustration, viz. If B Co. is subsidiary of A Co. and C Co. is subsidiary of B Co., C Co. will be subsidiary of A Co. If D Co. is subsidiary of C Co., D Co. also will be subsidiary of A Co. The definition is based on s. 154 of the English Act.

"*Officer in default*" (s. 5): Under the Act an officer of a Co. is liable to punishment and penalty (imprisonment, fine or both), if he is guilty of default in discharging his prescribed duties. In that connection the above expression means "an officer of the Co. who is *knowingly and wilfully* guilty of the default, non-compliance, failure, refusal or contravention of his prescribed duty or who *knowingly and wilfully* authorises the same". In other words, such officers can be prosecuted under the Act for breach of their prescribed duties only if the breach is deliberate, i.e. consciously and wilfully committed. "*Mens rea*", therefore, is always required to be proved.

"*Relative*" (s. 6): Two persons are deemed to be "relatives" if and only if, (i) they are husband and wife or (ii) if one or his spouse is related to the other, or to the other's spouse in any of the following ways: i.e., as parent or child, grand-parent or grand-child, brother or sister, uncle or aunt, nephew or niece, or as first cousins with common grand-parents, provided the last are members of a joint Hindu family, whether governed by the Mitakshara, Dayabhaga, Marumakatayam, Alyasantana or any other system of law. No distinction in this connection is to be made between legitimate and illegitimate descent, adoption, full blood and/or half blood.

This definition is an amplification of the meaning of "relatives", who are to be regarded as "associate" under s. 2 above. The above "relatives" of "managing agent" and/or "Secretaries and Treasurers", are to be treated as their "associates" for purposes of the provisions regulating the former's respective powers, functions and obligations. There is no counterpart to this in the English Act.

"*Person in accordance with whose directions or instructions the Board of Directors of Co. is accustomed to act*" (s. 7): does not include professional advisers, e.g. Solicitors, Pleaders, etc. in respect of advice given or services rendered by these as such.

Jurisdiction: The Court having jurisdiction for the purposes of the Act is the High Court having jurisdiction in relation to the place where the registered office of the company is situate. The Central Government may, by notification, also empower any District Court to exercise all or any of the jurisdiction conferred by the Act upon the High Court, in which case such "District Court" will be the "Court" for the purpose of jurisdiction under the Act, as regards companies having their registered offices in the district

(s. 10). The Central Government may place such restrictions, limitations and conditions on the District Courts, while conferring jurisdiction on them, as it thinks fit. Jurisdiction however cannot be conferred on the District Courts under ss. 237 (Order of investigation into Co.'s affairs), 391 (power to sanction compromise with creditors), 394 (power to sanction reconstruction and amalgamation), s. 395 (power to acquire shares of dissentient members) and ss. 397 to 407, both inclusive. (Powers of Court to relieve oppression of minority shareholders and mismanagement). Secondly, with regard to Co.s with a paid up capital of a lakh of more, no jurisdiction for winding up (under ss. 425 to 560), and other provisions of the Act can be conferred on the District Courts. The winding up of such companies must, therefore, be only by the High Court.

For the purpose of winding up, jurisdiction is placed on a different basis. For the purpose of winding up, the "registered office" of a company is to be deemed to be at the place where such office of the company has been situate for the longest period during the six months immediately preceding the presentation of the petition for winding up. The "Court" having jurisdiction in such place, therefore, will be the Court which will have jurisdiction to entertain a winding up petition (s. 10, cl. 3).

FORMATION OF A COMPANY

General Outline: Certain preliminary steps which are required to be taken for the formation of a company under the Companies Act are as follows: (i) persons desiring to trade together (not being less than 7, in case of public Co.s and not being less than 2, in case of private companies), have first to sign a Memo., called the "memorandum of association", which describes the object or objects for which the company is formed, its name and place of business, the liability which each member undertakes to take upon himself and the amount of capital with which it proposes to start business (s. 13). (ii) The Memo. must be registered with the Registrar of Companies and he will on such registration issue a certificate of incorporation (s. 33). (iii) Rules are framed for conducting the business of the company. These are called the "Articles of Association" of the Co. They provide for appointment of directors and managers, division of capital into shares of various classes and amounts, issue of share certificates, making of calls and declaring of dividends, calling meetings of members of the Co. voting at such meetings, and passing of resolutions of various kinds and all other matters relating to the internal management of the Co. (s. 28). (iv) The Co., if its first subscribing members are unable to find all the capital, issues a prospectus, inviting the public to subscribe for its shares (s. 55). (v) On applications for shares being made, shares will be allotted and these allottees will become the shareholders of the Co. (s. 69). (vi) The Co. carrying on business will enter into contracts and may also for the purpose of its business, borrow moneys on a mortgage of its properties. The documents evidencing such borrowing are called Debentures (s. 117). They are to be registered with the Registrar of Companies and they are also to be entered in a register kept by the Co. (ss. 125, 143). (vii) A balance sheet will be prepared every year after the Co.'s accounts are duly audited and it will be presented to the shareholders at the annual general meeting (s. 210). (viii) If there is a profit a dividend will also be declared. (ix) If the Co. is not able to carry on its business profitably, it may be wound up (s. 433). (x) Winding up may be (a) compulsory, or (b) voluntary, or (c) under supervision of Court (s. 425). (xi) A liquidator will be appointed to wind up the company (s. 448). (xii) He will settle a list of contributories of the company (s. 467) and will call upon them to contribute to the extent of the amount unpaid on their shares, if necessary (s. 470). (xiii) He will thereout pay the debts of the company, the debenture-holders naturally having priority and (xiv) if thereafter there is a surplus, he will distribute the same amongst the shareholders, and (xv) thus the Co. would be dissolved (s. 481).

Formation of a company: Under s. 12(i) any seven or more persons (and in case of a private company, any two or more persons), (ii) associated for any lawful purpose, may, (iii) by subscribing their names to a Memorandum of Association, and (iv) otherwise complying with the requirements of the Act in respect of registration, form an incorporated Co., with or without limited liability, that is to say either, (a) a Co. limited by shares, or (b) a Co. limited by guarantee, or (c) an unlimited Co.

The Act lays down stringent penalties for incorporated companies which carry on business with less than the minimum number of members prescribed above. Under s.

45, if at any time, the number of members of an incorporated company is reduced to below the prescribed minimum, and the Co. carries on its business for more than 6 months thereafter, every person who was member of the Co. after these 6 months and who was cognisant of the above fact shall be severely liable for the whole debts of the Co. contracted during that time and can be sued for the same, without joining any other member. When the number of members is reduced to below the legal minimum, the proper procedure is to wind up the Co., by means of a compulsory winding up (see s. 433). The requisite number of persons mentioned above must, further, combine for a "lawful purpose". Thus no Co. can be formed for carrying out a purpose which is not legal, e.g. running a lottery. These persons must put their signatures to the Memo. of Association. This is essential and is called the "subscription clause" of the Memo. It shows that the persons concerned have really consented to combine together to form a Co. They must, lastly, carry out the formalities prescribed by the Act for incorporation, e.g. paying the requisite fees, filing the Memo. and the Articles with the Registrar of Companies, etc. (see below).

Effect of Provisions of s. 11: The provisions of s. 12 are enabling provisions. Any seven (or two) or more persons may, if they so choose, by complying with the provisions of the Act, form a (public or private) incorporated Co. The Act, however, contains other provisions which make it obligatory, for certain kinds of associations, to be compulsorily registered under the Companies Act, in the manner laid down by the Act, before they can function as legal associations at all. These provisions are contained in s. 11 according to which (i) "no Co., association or partnership consisting of more than 10 persons shall be formed for the purpose of *carrying on the business of banking* unless it is registered under the provisions of this Act or is formed in pursuance of some other Indian Law and (ii) no Co., association or partnership consisting of more than 20 persons shall be formed for the purpose of *carrying on any other business* which has for its objects the acquisition of gain by the company, association or partnership or by any individual members thereof, unless it is registered as a company under this Act or is formed in pursuance of some other Indian Law."

The sec. is one of the most important in Company Law and has very far-reaching consequences. It is enacted in order to protect the public from being entrapped by mushroom Co.s. The effect of the sec. is that all associations or partnerships or combinations of persons must necessarily be registered under the present Companies Act (or under some other repealed Indian Companies Acts) wherever, (i) the number of members exceeds 10 in case of banking business, and (ii) exceeds 20, in case of any other business, "which has for its object the acquisition of gain". If they are not so registered as stated above, they will be considered in law as "illegal associations". The sec. in effect, makes all associations and partnerships, the number of whose members exceeds the number prescribed above, illegal, *unless* they are registered under the various Indian Companies Acts.

In order to come within the operation of s. 11, however, the following conditions are necessary: (i) There must be an "association". This implies that there must be in existence a combination of persons who have such legal relation between themselves as to give rise to mutual rights and obligations; (ii) The association, etc. must be formed for the purpose of carrying on a "business"; (iii) the business must have for its object the "acquisition of gain", and (iv) the number of members composing such association, etc. should exceed 10 in case of banking business and in cases of other businesses (having for their object the acquisition of gain), should exceed 20. All the above conditions must be satisfied, before an unregistered association can be called an "illegal association".

The mere fact that, as a result of a combination (which is not registered), some gain results to the members thereof, will not make that combination, an illegal association, if the combination is not made for the purpose of any "business". "*Business*" is a wider term than "trade". An association of persons who contribute sums to be applied for medical relief of members, the balance to be distributed at end of every year amongst the members, has been held not to be a "business" (e). "*Carrying on business*" only exists where there is a joint relation of persons for the common purpose of performing jointly

a succession of acts and not where the relation exists for the purpose of performing one act. A joint contribution by more than 20 persons, between whom no contractual relation exists, to subscribe to a fund to be invested in shares of Co.s by trustees for the subscribers, does not make the subscribers members of a Co. (f).

A "pool" agreement between various partnership firms (consisting of more than 20 members in all), for the purpose of eliminating unnecessary competition and for regulating prices, was not within the sec. so as to make the partnership, compulsorily registrable under the Companies Act (ff).

Associations, etc. which carry on business, but whose object is not the acquisition of "gain" are not compulsorily registrable. The expression "gain" has been held to refer to "acquiring" something, as distinguished from "spending" something. It is not limited to pecuniary gain or commercial profits (g). Thus associations formed for the purpose of promoting Art, Science, Religion or Charity, are not within the above rule and are therefore not compulsorily registrable (h).

The computation of the required number may present difficulties in particular cases. In this connection a joint Hindu family, as represented by its managing member, counts only as one person and it is not necessary to reckon each individual member of the family separately. This has now been made clear by cl. (3) of s. 11. Further where two or more joint families form a partnership, in computing the number of persons, for the purposes of the sec., minor members of such families should be excluded. The existence of a sub-partner, does not affect the number of members of a firm, for the purpose of s. 11 because a sub-partner is not a member of a firm (i).

It frequently happens that several firms (as distinguished from individuals), join together and form a big association for the purpose of trade. In such case, the association is treated as illegal, if the total number of individual members composing the several firms exceeds 20, though the number of firms joining together is below that number (*Senaji v. Pannaji*, 32 Bom. L.R. 1607). The restrictions laid down by s. 11 apply not only to the first formation of a company but they also rule its continuance. If a trading partnership, which is perfectly legal when started, subsequently has an increase in the number of its partners, beyond the limits prescribed by the sec., the association will become an illegal association and as such incapable of maintaining a suit (j).

Illegal Associations: It should be observed that an association consisting of more than the maximum number of members allowed by law, is an "illegal association", if it is not registered as required by s. 11. The law does not regard such association as having any legal existence. They are in the eye of Law, mere phantoms. The result of this is: (i) that such an association cannot enter into any binding contract (k). (ii) It cannot, also, enforce any contract, e.g. a contract by a promoter in favour of such an association, cannot be enforced by it (l). (iii) Such an association cannot be dissolved through the Court (m). Under s. 11 of the Act the following further consequences also follow, where an unregistered, i.e. an illegal association, carries on business without getting itself registered as required by the Act. In such a case, every member of such a company, association or partnership, shall be personally liable for all liabilities incurred in such business and every member shall also be liable to a fine, not exceeding Rs. 1,000. An association of more than 20 persons, if unregistered, is invalid at its inception, and cannot be made valid by subsequent reduction in the number of members to below 20 (n), nor can a contract made by such illegal association, before registration, be made valid and be sued upon by subsequent registration (o). S. 631 of the Act makes it punishable for any person or persons, to trade or carry on business under any name or title of which "limited" is the last word, without being fully incorporated, i.e. registered with limited or unlimited liability.

(f) *Smith v. Anderson* (1880), 15 Ch.D. 247.

(ff) *New Mofussil Co. Ltd. v. Rustomji*, 38 Bom. L.R. 408.

(g) *Tan Waing v. Bo Hein*, 10 Rang. 490.

(h) *The Arthur Average Ass.*, 10 Ch. 545.

(i) *Chandulal v. Keshavlal*, 38 Bom. L.R. 486.

(j) *Rajashahi Banking Corp. v. Pulin*

Behari, 42 Cal. W.N. 610.

(k) *Jennings v. Hammond* (1882), 9 Q.B.D. 225.

(l) *Shaw v. Benson*, 11 Q.B.D. 563.

(m) *Mewa Ram v. Ram Gopal*, 48 All. 735.

(n) *Madanlal v. Jankiprasad*, 49 All. 319.

(o) *Gujiat Trading Co. v. Tricumji*, 3 Bom. H.C.R. (O.C.) 45.

Though an association may be illegal, however, it does not follow that moneys paid in respect thereof cannot be recovered or that accounts of moneys paid to it cannot be asked for. In an English case, an unregistered association, with four branches, each with more than 20 members, was formed with the object of collecting subscriptions from members of each branch and to lend the same to members at interest. Each fund was also to be periodically divided up among its members in a certain rateable manner. *Held*, the association was illegal as it had for its object, the acquisition of gain, but that, notwithstanding the same, the members could, before the illegal object was carried out, ask for an account of the moneys paid by them, from the directors, secretaries and agents of the association who were their agents (p). The opinion was also expressed in this case that the court would order a refund of the moneys so paid, provided the illegal purpose had not been carried out. The defence of illegality is not open to the company in an action against it by an innocent stranger. The reason is that to allow the company to do so would be to allow the company to take advantage of its own wrong.

Registration under the Companies Act and Partnership Act distinguished: (i) The Partnership Act requires all partnerships formed after October 1933 (irrespective of the number of their members), to be compulsorily registered. The Companies Act requires only partnerships and associations of persons exceeding certain number to be compulsorily registered. (ii) Under the former Act, registration is with the Registrar of Partnerships, under the latter Act, with the Registrar of Companies. (iii) Registration under the former Act does not give corporate existence to the partnership. Registration under the latter Act does. (iv) The consequence of non-registration under the former Act is only this, that such a partnership will not be allowed to file a suit till it is registered (which can be done at any time). Under the latter Act, the result of non-registration, when necessary, is that the Co. becomes an illegal association altogether. (v) The object of registration under the two Acts is different. Registration of the names of partners under the former Act is made obligatory, in order to avoid, if possible, a subsequent dispute as to who the partners were. Registration under the Companies Act is an integral part of the process of formation of a Co., because without it, the company does not obtain a corporate existence.

Requirements to be gone through before Incorporation is complete are as follows: the parties subscribing to the Memo. must file with the Registrar of Companies: (a) the Memo. of Association; (b) the Articles of Association (except where Table A is adopted as the Articles of the Company (s. 33); (c) the agreement (if any) which the Co. proposes to enter into with an individual, firm, or body corporate, to be appointed its managing agent or secretaries and treasurers; (d) (except in the case of a private Co.) a list of persons who have consented to be the directors of the company together with the consent in writing of each of such persons to act as such director and pay for his qualification shares (the last statement is not required to be filed when the company is limited by guarantee and has no share capital) (s. 266); (e) a declaration under s. 33 by an advocate, attorney or pleader entitled to appear before the High Court or a Chartered Accountant or by any director, manager or secretary that all the requirements of the Act have been complied with; (f) on such documents being filed with the Registrar and the requisite fees duly paid; (g) the latter issues a certificate known as "*Certificate of Incorporation*". This Certificate is, by s. 35 of the Act, made *conclusive evidence* that all the requirements of law regarding registration have been duly complied with. The Co., however, is still not entitled to commence business. Before it can do so, it has, if a public Co., to secure a "*certificate of commencement of business*" from the Registrar, which will be granted only after (i) shares payable in cash, equal to "minimum subscription" amount have been allotted, (ii) every director has paid to the company on shares taken up by him, the amount payable on application and allotment, and (iii) a verified declaration signed by the Secretary or one of the Directors has been duly filed with the Registrar (s. 149).

MEMORANDUM OF ASSOCIATION

Importance of Memorandum: As was pointed out by Lord Cairns as far back as 1875 in *Ashbury Railway Company v. Riche* (q), "the memorandum of association of a

(p) *Greenburg v. Cooperstein* (1926) Ch. 657, followed in *Ramdas v. Mukutdhari*,

A.I.R. 1952 V.P. 1.
(q) L.R. 7 H.L. 688.

company is its charter and defines the limitations of the powers of the company, established under the Act". "The memorandum contains the fundamental conditions upon which alone the company is allowed to be incorporated" (r). The Memo. of Association of a Co. is the most important document with regard to its constitution. It is the foundation on which the whole structure of the company is built up. Its purpose is twofold: "The first is that the intending incorporator who contemplates the investment of his capital shall know within what field it is to be put at risk. The second is that anyone who shall deal with the Co. shall know without reasonable doubt whether the contractual relation into which he contemplates entering with the Co. is one relating to a matter within its corporate objects" (s). The result is that a Co. cannot depart from the provisions contained in its Memo., however great the necessity may be. Thus it cannot enter into contract or engage in any trade or business, which is beyond the powers conferred on it by the Memo. If it does, it would be "*ultra vires*" the company and therefore wholly void and inoperative. The second result of this position is that a Co. cannot alter the provisions of its Memo., however unanimously it may desire to do so and however beneficial the alteration may be, unless the special conditions laid down by the Act are fulfilled and the special procedure prescribed by the Act is followed.

Contents of Memorandum: There is no restriction in law as regards the clauses which a Memo. of association of a Co. may contain. Sec. 13 however prescribes the clauses, which the Memo. of every Co. incorporated under the Act, must contain: They are the minimum, without which a Co. cannot be registered. These cls. are generally known as (i) the "Name clause", (ii) the "Registered Office clause", (iii) the "Objects clause", (iv) the "Liability clause", (v) the "Capital clause" and lastly (vi) the "Association clause".

Under s. 13 the Memo. of a *company limited by shares* shall state: (i) the name of the company with "limited" as the last word in its name if a public Co., and the words "Private Ltd." if a private Co. (ii) The State in which its registered office is to be situate. (iii) The objects of the Co. and (except in cases of trading corporations), the State or States to whose territories the objects extend. (iv) That the liability of the members is limited, and (v) the amount of the share capital with which the Co. proposes to be registered and the division thereof into shares of fixed amounts. The sec. further provides that no subscriber to the Memo. shall take less than one share and each subscriber shall write opposite to his name the number of shares he takes.

In the case of a *company limited by guarantee*, the sec. provides that its Memo. shall state: (i) the name of the Co. with the word "Limited" as the last word in its name; (ii) the State in which the registered office of the Co. is to be situate; (iii) the objects of the Co., and except in the case of trading corporations, the State or States to whose territories the objects extend; (iv) that the liability of the members is limited; (v) that each member undertakes to contribute to the assets of the Co., in the event of its being wound up, while he is a member or within one year afterwards, for payment of the debts and liabilities of the company, or for such debts and liabilities of the Co. as may have been contracted before he ceased to be a member, and of the costs, charges, and expenses of winding up and for adjustment of the rights of the contributories amongst themselves, such amount as may be required, not exceeding a specified amount. Notice in this connection that under s. 37 of the Act, a provision in the Memo. (or articles or resolution) of a guarantee Co., registered on and after 1st April 1914 and not having a share capital, purporting to give a person a right to participate in the divisible profits of the Co., otherwise than as a member shall be void. The sec. further provides that for the purposes of the Act and the sec. itself, a provision in the Memo. (or articles or resolution) of a guarantee Co. of the above type, purporting to divide the undertaking of the company into shares or interest shall be treated as provision for share capital, although neither the nominal amount or number of the shares or interest are specified. If the Co. has a share capital, (i) the Memo. shall also state the amount of share capital with which the company wants to be registered and the division thereof into shares of a fixed amount. (ii) No subscriber to the Memo. shall take less than one share. (iii) Each subscriber shall state opposite to his name the number of shares he takes.

(r) *Ashbury v. Watson* (1885), 28 Ch.D. 56.

(s) *Cotman v. Brougham* (1918) A.C. 514.

In the case of an *unlimited company* the sec. provides that its Memo. shall state: (i) the name of the Co., (ii) the State in which its registered office is to be situate, (iii) the objects of the Co. and (except in the case of trading corporations), the State or States to which their objects extend. If the Co. has share capital, (iv) no subscriber to the Memo. shall take less than one share, and (v) each subscriber shall state opposite to his name the number of shares he takes.

Clauses of the Memorandum: Name Clause: A Co. may select any name for itself that it likes, subject, however, to the following: In cases of Co. with limited liability the word "Limited" must appear as the last word in its name. This is necessary as it gives distinct notice to all persons dealing with the Co., that the liability of its members is a restricted liability only. The only case where the word "Limited" is permitted to be dropped from the name of a limited Co. is under s. 25 with regard to associations formed for the purpose of promoting Art, Science, Religion, etc. These associations being not intended for profit, it is assumed that, generally, persons dealing with such a Co., will not be misled by the absence of the word "Limited", from their name (see *seq.*).

The Memo. shall be in one of the forms in Tables B, C and D to 1st Schedule or in a form as near thereto as circumstances admit (s. 14). The Memo. shall be printed, divided into consecutively numbered paras and shall be signed by each subscriber, with his address, description and occupation added, in the presence of at least one witness who will attest the same (s. 15).

No Co. shall be registered by a name which, in the opinion of the Central Government, is undesirable. A name which is either identical with or which too nearly resembles, the name by which a Co. in existence has already been registered, may be deemed to be undesirable by the Central Government (s. 20). The whole discretion as regards sanctioning the name with which a Co. should be registered is now vested in the Central Government. "Undesirable" is nowhere defined in the Act. It may be presumed however that names containing words like "Crown", "Empire", "Government", "Municipality", if having tendency to imply a patronage of such bodies, would be regarded as "undesirable". Generally, no Co., association or partnership can trade with a name identical or similar to that of an already existing Co., association or partnership so as to deceive the prospective customers of one, into trading with the other. This is called "passing off", and is prohibited by the general law, apart from the special provision of the Companies Act (t).

If, through inadvertence or otherwise, a Co. is registered by a name, which, in the opinion of the Central Government, is either identical with or too nearly resembles the name of an already registered Co., the first mentioned Co. (a) *may*, by ordinary resolution, and with previous sanction of Central Government (signified in writing), change its name, (b) further, the first mentioned Co. *shall*, if the Central Government, so directs within 12 months of its registration or within 12 months of the commencement of the Act (whichever be later), by ordinary resolution, with previous sanction of the Central Government (signified in writing), change its name, within 3 months of such direction or such longer time as the Central Government may allow. Default in carrying out the direction of the Central Government is punishable with a fine (upto Rs. 100) for every day the default continues (s. 22).

Where a Co. changes its name in any of the above ways, the Registrar shall enter the new name in the register and shall issue a new certificate of incorporation with the necessary alterations and it is only on such certificate being issued, that the change of name becomes legally effective. The Registrar shall make similar alterations in the Memo. also. The change of name, however, will not affect any rights or obligations of the Co. or render defective any legal proceedings by or against the Co., which can be instituted or continued by or against the Co. by its new name (s. 23).

Registered Office Clause: This cl. is important for determining the court within whose jurisdiction proceedings with regard to the Co. would be brought. It is also important for the purpose of ascertaining the domicile and nationality of a Co., i.e. whether the Co. is an Indian or foreign Co. The reason for requiring the Co. to have a registered office is to fix the place where notices or other documents connected with Co.'s administration, can be respectively sent or inspected (see *seq.*).

(t) *Tussaud v. Tussaud* (1890) W.N. 78.

Objects Clause: This cl. defines the objects of a Co. and is often called the "objects clause". This is the most important clause in the Co.'s Memo., because it not only shows the object or objects for which the Co. is formed but it also determines the extent of the power and authority which the Co. can exercise, in order to achieve the object or objects. The cl. thus serves two important purposes. As Lord Cairns puts it in *Ashbury Railway Co. v. Riche* (u), it "states affirmatively the ambit and extent of vitality and power which by law are given to the corporation, and it states, if it is necessary to state, negatively that nothing shall be done beyond that ambit and that no attempt shall be made to use the corporate life for any other purpose than that which is so specified". The result is twofold: (i) a Co. cannot enlarge or modify the statement of the objects contained in the Memo. except in certain cases; (ii) it cannot also go beyond them.

The subscribers to the Memo. may choose any "object" or "objects" for the purpose of their Co. There are two restrictions, however, on the selection of "objects" for a Co.: (i) the objects should not include anything which is illegal or contrary to law or public policy, e.g. floating a company for dealing in lotteries (v); or for trading with alien enemies (w); and (ii) the objects should not contemplate doing anything which is prohibited by the Companies Act, e.g. buying the Co.'s own shares. Apart from these two restrictions, the objects of a Co. may be anything that the proposed Co. desires to achieve.

Doctrine of "Ultra Vires": As pointed out before, it is a fundamental rule of Company Law that the objects of a company as stated in its Memo. cannot be departed from except so far as the Act permits of a change in them (x). The result is that, any act done or any contract made by the Co., which goes beyond the Memo. or which is not expressly or impliedly warranted by it, is *ultra vires* (i.e. beyond the powers of), not only the directors but of the Co. itself. The consequence is that such an act or contract is wholly void and inoperative in law, and will not therefore be binding on the Co. Thus employing funds of a Co. for purposes other than those sanctioned by the Memo. is *ultra vires* the Co., and the Co. will therefore be restrained from doing so (y). The doctrine has been carried to this extent that if the particular act or contract is *ultra vires* the Co., even the whole body of shareholders, cannot by subsequent ratification make it valid and binding on the Co. This is because the Memo. of a Co., as framed, is the sole charter, defining and limiting the Co.'s area of operation and anything that goes beyond it is therefore totally void and of no effect. Thus a Co. formed to carry on one trade cannot carry on another (z). Where a Co. by its Memo. was incorporated with the object of making and selling railway carriages and all other kind of railway machinery and generally to carry on the business of mechanical engineers and general contractors, held the purchase of a concession, to erect a railway in a foreign country and an assignment thereof to a new Co. formed therein, who was to supply materials and receive payments from the English Co. was *ultra vires* the Co. (a). So also an authority to a County Council to run trams does not empower it to run omnibuses (b). A Railway Co. cannot subscribe to the Imperial Institute (c). In India making gifts to Gandhi Fund was validated by Act 35 of 1948. This Act has been repealed by the Companies (Donations to National Funds) Act (54 of 1951) under which Co.s in India are allowed by extraordinary resolution, to use the Companies' Funds for making donations to the Gandhi National Memorial Fund, Sardar Vallabhbhai National Memorial Fund or any other Fund for charitable purpose which has been approved by the Central Government by reason of its national importance.

There are, however, certain exceptions to the rule: (1) If the act is "*ultra vires*" the power of the directors only (e.g. their borrowing powers), as defined by the articles, the shareholders can ratify it. (2) If it is "*ultra vires*" the articles of the Co., the Co. can alter its articles in the proper way and rectify the error. (3) If the act is within

(u) L.R. 7 H.L. 653.

(v) *Ex parte More* (1931), 2 K.B. 197.

(w) *Daimler & Co. v. Continental Tyre Co.* (1916), 2 A.C. 307.

(x) *Ashbury Rly. Co. v. Riche* (supra).

(y) *Angostura Bitters Co. v. Kerr* (1933) A.C. 550.

(z) *Egyptian Salt and Soda Co. v. Port Said Salt Asso.* (1931) A.C. 677.

(a) *Ashbury Rly. Co.'s case* (supra).

(b) *Att. G. v. London County Council* (1902) A.C. 105.

(c) *Tomkinson v. S.E. Rly.* (1887), 35 Ch.D. 657.

the powers of the Co., but it is done irregularly, consent of all the shareholders will validate the act (d). The consent need not be given at the same meeting or the same place (e). (4) The Co.'s rights over property, will be protected, even though the property has been acquired by "ultra vires expenditure", e.g. where telephone wires of a Co. were cut and the Co. had no power in the Memo. to put up the wires, the Co. was still held entitled to recover damages for the injury (f). (5) The doctrine of "ultra vires" has also to be reasonably applied and what is fairly incidental to or consequential upon that which is authorised by the Memo. will (unless expressly prohibited), be held to be "intra vires" (g). Thus a Co. bound to supply boats for a ferry may employ the boats, when not wanted for the said purpose, for excursions (h). A Co. formed to work a patent may use its funds to purchase the patent (i). A Co. formed to work mines leased by it, may buy the freehold including the surface (j). In *Foster v. London, Chatham and Dover Railway Co.* (k), a railway Co. which was authorised to acquire land to erect railway was held to have power to let out the arches, on which the railway was erected, for use as workshops. Still more recently a railway Co. has been held to have power to grant an option for lease of a refreshment room at a railway station (l). An option for lease for 999 years, however, will be bad (m). (6) There are certain powers which are often implied by law, in case of Co.s: Thus a trading Co. has implied power to borrow, and also it has been held, to sell land (n). Powers to borrow, raise money and give security of its property are held to be implied in case of a trading Co. (o). Where a Co. had power to "subsidise and assist other Co.s, held, guaranteeing debentures of another Co. was "intra vires" (p). In a recent case it was held by the Bombay High Court that where a joint-stock Co. is, by its Memo., given absolute power to purchase land, it is implied, as a part of its constitution, that it has power to let the land or if necessary, also to sell it (q). Notice further that where the Memo. specifically states that each of the objects mentioned therein is an independent principal object of the Co., the Court will treat each object as the principal object of the Co. and the rule as regards the "main" or "dominant" object, will not apply (r). (7) There may be a power given to a Co., impliedly, by the Memo. itself. Whether a Memo. impliedly gives such a power in fact, is a question to be decided according to the circumstances of each case. Thus, where a Co.'s Memo. authorised the Co. to purchase gold mines "in Mysore and elsewhere", it was held that under the last words, the Co. had power to purchase and work gold mines in Bombay (s). On the other hand, in another case, where similar words were used, it was held that the words did not empower a Co. to purchase an option with a view to form a new Co. to work mines on the Gold Coast (t). (8) Though the act is "ultra vires" rights arising independently thereof are not affected thereby. Thus in a recent case where in consideration of the plaintiff advancing £1,500 to the Co., a guarantee was given by two directors of the Co., who were also the shareholders thereof, to the effect that the Co. would re-purchase certain shares purchased by the plaintiff, and secure the payment of the price thereof by accepting bills of exchange of an equal amount from the plaintiff, and the agreement by the Co. to re-purchase its own shares was held "ultra vires" the Co., it was held that the plaintiff could still recover against the directors on their guarantee (u).

Association clause: The last cl. in the Memo., is the "association clause". Those who had agreed to subscribe to the Memo. must signify their agreement to associate and form a Co.

(d) *Express Engineering Works Ltd.* (1920), 1 Ch. 406.

(e) *Parker & Cooper Ltd. v. Reading* (1926) Ch. 975.

(f) *National Telephone Co. v. Constables of St. Stephens Port* (1900) A.C. 317.

(g) *Attorney General v. G.E. Rly. Co.* (1880), 5 App. C. 473.

(h) *Forrest v. Manchester Rly. Co.* (1861), 39 Beav. 40.

(i) *Leitchfield's case* (1865), 1 Eq. 231.

(j) *Johns v. Balfour* (1889), 5 T.L.R. 389.

(k) *Foster v. London Chatham & Dover Rly. Co.* (1895), 1 Q.B. 711.

(l) *County Hotel Co. v. L.N.W. Rly.*

(1918), 2 K.B. 251.

(m) *Ibid.*

(n) *Re Kingsbury Colliery Co.* (1907), 2 Ch. 259.

(o) *General Auction Co. Ltd. v. Smith* (1891), 3 Ch. 432.

(p) *Re Friary* (1922) W.N. 293.

(q) *Gujrat Ginning Co. v. Motilal*, 31 Bom. L.R. 1310.

(r) *Cotman v. Brougham* (supra).

(s) *Pedler v. Road Block Gold Mines Ltd.* (1905), 2 Ch. 127.

(t) *Stephen v. Mysore Gold Reefs Ltd* (1902), 1 Ch. 745.

(u) *Gerrard v. James* (1925) Ch. 616.

Subscription to the Memo.: This is the signature of the various subscribers to the Memo. It must be put in the presence of one witness, who shall attest the same (s. 15). The subscriber as well as the witness must also add their respective addresses, designations, and occupations, if any. Each subscriber must also write opposite to his name the number of shares he takes. This makes the signatories, members of the company, without more (see post). According to s. 12 of the Act, at least 7 persons are necessary to sign the Memo. in case of a public Co., and at least two in case of a private Co.

Extent of the interest of Subscribers to the Memo.: So far as law is concerned the extent of the interest of the seven persons constituting the Co., as also the motives that prompt them to take up shares and their relations "*inter se*", are immaterial and do not affect the validity of the company. Of the seven, one may hold all the shares, leaving one share to each of the other subscribers to hold. The remaining six may themselves hold their shares as trustees for the seventh. These things, however, will not invalidate the Co., the Court not going out of its way to inquire into the motives and schemes of the parties forming the company (v). Anybody can be subscriber to a Memo. In England it has been held that even a minor can subscribe (w), his contract being voidable. A foreigner also can subscribe to a Memo., and it has been held that it does not matter that all the subscribers to a Memo., are foreigners, provided the business or management of the proposed Co. is to be carried on in England (x).

Duties of Subscribers of the Memo.: They are: (i) to pay for the shares they have subscribed, (ii) to sign the Articles of Association, if any, (iii) to appoint the first directors, and (iv) to act as such directors till the first directors are appointed (if the Articles so provide). Their further duties are to file the necessary documents with the Registrar and get the company registered.

Act to override Memo.: Under sec. 9 anything contained in the Memo. (or articles or in any agreement executed by the Co. or in any resolution passed by the Co. in general meeting or by the Board of Directors of the Co.) and whether the same is registered (executed or passed) before or after the commencement of the Act, shall, to the extent to which it is repugnant to the provisions of the Act, be void and the provisions of the Act shall prevail notwithstanding the same.

Alteration of the Memorandum

As already pointed out earlier, the Memo. of a Co. being its fundamental charter, the Co.'s right to alter its contents, is rigidly limited by the provisions of the Act. Not only can a Co. not depart from the powers given to it by the Memo., but it cannot also alter the conditions of the Memo., "except in the cases and in the mode and to the extent for which express provision is made in this Act" (s. 16). Much difficulty has arisen in construing the word "condition" used in the sec. Does it include all the terms of the Memo. or those only, which relate to the main objects of the company? This is now clarified by s. 16 of the present Act, according to which only those provisions which are required by s. 13 or by any other specific provision of the Act to be stated in the Memo. are to be deemed to be "conditions". Other provisions contained in the Memo. including those relating to the appointment of a managing director, managing agent, secretaries and treasurers, or manager, are not to be regarded as "conditions". They therefore can be altered in the same way as articles or in any other special way provided in the Act. The sec. further makes it clear that such provisions as above (which are not "conditions"), shall be treated as articles and shall be governed by all the provisions of the Act relating to articles. It follows therefore that a clause in the Memo., relating to the appointment of a managing agent or manager, can be altered by the Co., without it being necessary for the Co. to go through the special procedure prescribed by ss. 16-17 of the Act. This in fact was held to be so, by the Bombay High Court, even before the present Act was passed in *Ramkumar Potdar v. Sholapur Spinning & Weaving Co. Ltd.* (y), where their Lordships held that a cl. in the Memo. providing that "the firm of Morarji Goculdas and Co. or whatever member or members, that firm may, for the time being, consist of, shall be the agents of the Co., so long as the said firm shall carry on business in Bombay or until they shall resign" could be altered, modified or rescinded by the Co., by a proper resolution, as the cl. did not fall within the "objects

(v) *Saloman v. Saloman & Co.* (supra).

(w) *Re Laxon and Co.* (1892), 3 Ch. 555.

(x) *R. v. Arnand* (1846), 9 Q.B. 806.

(y) 36 Bom. L.R. 907.

clause" of the Memo. but merely imposed on the Co. an obligation as to the internal management of the Co. The Court also relied on the fact that the agency firm could not be considered to be a corporation sole, having a perpetual succession and hence when new partners were added, a new firm came into existence with which the Co. never had any contractual privity.

Cases in which alteration of Memo. is Allowed: There are certain cases in which the Act allows alteration of the Memo. (1) *Change of Name:* (i) Under s. 22, if a Co. through inadvertence or otherwise, registers under a name identical with that of a Co. in existence, which is already registered, or so nearly resembling it, as to be calculated to deceive, the first Co., may by ordinary resolution, with the previous approval of the Central Government, change its name. It is also bound to change its name if so directed by the Central Government within 2 months of its registration or within 12 months of the Act coming into operation (whichever is later), as provided by s. 22 (*see ante*).

(ii) Under s. 21, a Co. may also, by passing a special resolution, and with the approval of the Central Government in writing, change its name.

(2) *Change of Registered Office:* Under s. 17, cl. (1), a Co. may, by a special resolution, alter the provisions of its Memo. so as to change the place of the registered office of the Co. from one State to another. Such alteration however cannot take effect until and except in so far as it is confirmed by the Court.

Certified copy of the Court's order, sanctioning the change, and a printed copy of the Memo. as altered must be filed with the Registrar within three months of the order or within such further time as the Court may allow (s. 18). The Registrar shall register the same and issue a certificate of registration which shall be conclusive evidence that all the requirements of the Act as regards alteration and confirmation thereof have been complied with and thereafter the Memo. as altered, shall be the Memo. of the Co. Where the alteration involves change of registered office from one State to another, a certified copy of the Court's order must be filed with each of the Registrars and each of them must register and certify the registration of the same. If registration is not effected within three months of the order of the Court, or such further time as the Court may give, the alteration and the whole proceedings therefor shall be null and void (s. 19), provided that on sufficient cause being shown, the Court may revive the order on application made within a further period of one month.

(3) *Change of "objects":* A Co. has no unfettered right to alter the "object clause" of the Memo., however urgent or beneficial such alteration may be. Only a limited right is given to a Co. by s. 17 of the Act, to alter its "objects clause". Under the sec., a Co. can alter its "objects clause" for the following purposes only and no other, i.e. (i) to carry on its business more economically or efficiently; (ii) to attain its main purpose by new or improved means; (iii) to enlarge or change the local area of its operations; (iv) to carry on some business which under the existing circumstances may conveniently or advantageously be combined with the business of the company, or (v) to restrict or abandon any of the objects specified in the memorandum; (vi) to sell or dispose of the whole or any part of the undertaking or undertakings of the company; and (vii) to amalgamate with any other company or body of persons. The result is that a Co. can alter its "objects clause" only to the above extent and only for the above named purposes. If the proposed alteration does not fall within any of the relevant cls. of s. 17, the fact that the Co. has approved it by a special resolution or has even unanimously approved it, will not give jurisdiction to the Court to sanction it.

The question to be considered, therefore, when any alteration in the "objects clause" of a Memo. is desired, is whether the proposed alteration falls within any of the cls. of s. 17. In this connection, where a Co. was incorporated for the purpose of investment and loans and it was found that the business of the Co. could be more conveniently carried on with less restricted borrowing powers and that additional powers of a guarantee and finance Co. would enable the company to carry on business more efficiently, an alteration of the Memo. was allowed (z). Where a Co. was incorporated for underwriting on cargo and freight, an alteration of the Memo. was allowed so as to include assurances

on ship's respondentia, bottomry and risks in transit on land (a). Similarly, a marine insurance Co. has been allowed to alter its Memo. by adding fire, life and accident assurance to its business, it being proved to the Court, that the proposed addition would be advantageous to the existing business of the Co. (b). Where, however, a Co. was incorporated for the purpose of assisting and protecting riders of bicycles, on public roads, a proposed alteration of the Memo. to include all vehicles, including motor cars, was disallowed. "The alteration in the memorandum contemplated is an alteration which will leave the business of the company substantially what it was before, with only such changes in the mode of conducting it as would enable it to be carried on more economically or more efficiently" (c). Here one of the dangers which the Co. was formed to protect against, were motor-cars themselves. Including these last in the Memo., therefore, would be inconsistent with the object of the Co. Where a Co. was incorporated with the object of investing in a stock of particular denomination, and by reason of a fall in prices of this stock and by reason of outside competition, the business could not be carried on advantageously, sanction was given to alter the Memo. so as to include stock of other denominations (d). It has been recently held by the Calcutta High Court (dd) that contribution from Company's Funds to a political fund or for political objects, is not prohibited by the Act and is therefore perfectly "lawful". An amendment of the Memo. for such purpose is therefore permissible, if necessary to carry on the Co.'s business more "economically" or "efficiently" under s. 17(a). Under the present Act a Co. can alter its Memo. so as to include amongst its objects, a power to sell or dispose of the whole undertaking of the Co. or a power to amalgamate with another Co. or body of persons. S. 17 enables the Co. to alter, not only the "objects clause" of the Memo. but, as has been held in England (e), all other cls. also in the Memo., which have reference to the "objects" of the Co.

It will be observed that s. 21 provides for alteration of the name cl. in the Memo., while s. 17 provides for the alteration of the registered office cl. and the "objects clause" in the Memo., to a certain extent. There are other secs. in the Act (see below) providing for alteration of the capital clause and also the liability clause in the Memo., in certain cases. Excepting these specified cases, can other clauses in the Memo. which have no reference to the "objects" of the Co. be altered by the Co. and can any such alteration, if made by the Co. be sanctioned by the Court? In this connection it has been held that the provisions in the Memo. fixing the rights of preference and ordinary shareholders cannot be altered by the Co. or by the Court as they are the "conditions" under which company is formed (f). Notice, however, that where the Memo. itself lays down the conditions under which rights attached to any class of shareholders can be varied, a variation of such rights accordingly does not require a special resolution because it does not amount to a variation of the conditions of the Memo. (g). Similarly it has been held that a cl. in the Memo. relating to the limited liability of members is not a clause with regard to the "objects" of the company and therefore cannot be altered under these provisions (h). In such cases the answer would now seem to depend on the true construction of the amended s. 16. If the alteration is not permissible under any sec. of the Act, the only remedy is to seek a dissolution of the Co. before the desired alteration can be effected.

Procedure for alteration of "objects" cl. (s. 17): Before the Co. can change its "objects clause" it is necessary (i) that the Co. should pass a special resolution sanctioning the alteration. (ii) A petition has then to be made to the Court to confirm the alteration. (iii) The Court, before it confirms the alteration, must be satisfied that (a) sufficient notice has been given to every debenture-holder of the Co., and all persons whose interests will be affected by the alteration (the Court, in case of any person or class, may, for special reason, dispense with the notice); and (b) that every creditor

(a) *Re Ulster Marine Ins. Co.*, 27 L.R. Ir. 487.

(b) *Re Alliance Marine Ass.* (1891), 1 Ch. 300.

(c) *Re Cyclists Touring Club* (1907), 1 Ch. 269.

(d) *Re Govt. Stock Investment Co.* (1892), 1 Ch. 597.

(dd) *Re Tata Iron and Steel Co.*, A.I.R.

(1957) Cal. 234.

(e) *Re Incorporated Glasgow Dental Ass.*

(1927) A.C. 400.

(f) *Ashbury v. Watson* (1885) 30 Ch.D. 376.

(g) *Re India Corp. Ltd. v. Shanti Narayan*

(1935) A.L.J. 527.

(h) *Re Society for Welfare of Women*, 71 L.J. 583.

of the Co., who objects to the alteration, has been paid off or secured or his consent to the alteration has been obtained. (iv) The Court, in confirming the alteration, must have regard to the rights and interests of the members of the Co. as well as to the rights of all the classes of the creditors of the Co. (v) The Court may, if it thinks fit, adjourn the proceedings, in order that a satisfactory arrangement may be arrived at for buying up the interests of the dissentient members and may give all directions, orders and facilities as are necessary, to carry out the arrangement, provided always that no part of the capital of the Co. is used for such purchases. (vi) The Court must also consider, whether the proposed alteration in the objects is allowed by s. 17. (vi) After having considered all the above matters, the Court may make an order confirming the alteration, either wholly or in part, and on such terms and conditions as it may think fit. (vii) The Court in one case before approving an extension of the objects of the Co. required the Co. to alter its name (i). (viii) The Court can also make such order as to costs as it may think proper. (ix) Before confirmation of the alteration by the Court, notice of the proposed alteration must be given to the Registrar, and he should be given reasonable opportunity to appear before the Court and state his objections and suggestions regarding confirmation of the alterations.

Procedure on confirmation of alteration (ss. 18-19): On confirmation of the alteration by the Court, a certified copy of the order confirming the alteration, together with a printed copy of the Memo., should be filed by the Co. with the Registrar within three months of the date of the order. The Registrar will register the same and certify the registration under his hand. The certificate shall be conclusive evidence that all requirements of the Act with respect to alteration and confirmation have been complied with. Thereafter the Memo. as so altered shall be the Memo. of the Co. Where the alteration involves a transfer of the registered office of the Co., from one State to another, a certified copy of the confirmation order must be sent to the Registrar of each State. Each Registrar shall register the alteration and certify the same under his hand. The Registrar of the first State must forward all documents and records of the Co., filed with him, to the Registrar of the other State. The Court may, by order, at any time, extend the time for filing the above document with the Registrar for such period as the Court thinks proper. No such alteration will have any operation until registered as above, and if the alteration is not registered within three months next after date of the order or such further time as the Court may allow, such alteration and order and all proceedings connected therewith shall become void. The Court may, however, on sufficient cause being shown, revive the order if an application for the purpose is made within a further period of one month.

Dispensing with the word "Ltd." in the name of the Co. (s. 25): Under the sec. where it is proved to the satisfaction of the Central Government that an association is (i) about to be formed as limited Co. for promoting commerce, art, science, religion, charity or any other useful object and that (ii) it intends to apply its profits (if any) or other income in promoting its objects and (iii) to prohibit the payment of any dividend to its members, the Central Government may, by licence, direct that the Association may be registered with limited liability, without the addition of the word "Ltd." to its name. Such an Association may thereupon be registered accordingly and on registration shall enjoy all the privileges and be subject to all the obligations of limited Co.s. On the above conditions being fulfilled, the Central Govt. can also authorise a Co., by licence, to make a change in its name by omitting the word "Ltd." or "Private Limited" therefrom, by passing a special resolution to that effect. The provisions of s. 23 shall apply to such change also.

The Central Government may grant the licence on such terms and conditions as it may think fit and the same shall be binding on the body to whom the licence is granted. In case of the first formation of such Co. the Central Government may require such terms and conditions to be inserted in the Memo. or Articles or both. The effect of the licence is to exempt the body, (i) from the use of the word "Ltd." and "Private Limited" as part of its name, (ii) from publishing its name, and (iii) if the Central Government allows and to the extent it allows (a) from sending a list of its members to the Registrar and (b) from keeping a register of its directors, etc. under s. 303. The licence can be revoked by the Central Government at any time, after notice to the body,

of its intention to do so, and after giving it an opportunity of being heard against such revocation. On revocation of licence, the body in question shall cease to enjoy the above exemptions and the Registrar shall enter the word "Ltd." or "Private Limited" against its name in the Register. Where such a licensed body alters its objects, the Central Government may (i) revoke the licence if it thinks fit or (ii) vary the terms and conditions of the licence in any manner it thinks fit.

Where a licence is granted to a body whose name contains the words "Chamber of Commerce", that body shall within 3 months from date of revocation of the licence (or such further time as may be allowed) change its name to a name which does not contain those words. The notice to be given to such body before revocation of the licence shall contain statement setting out the above provisions. S. 23 shall apply to such a change of name also. If the body in question fails to carry out the above requirements it is liable to a fine extending to Rs. 500 for every day the default continues. Nothing in the sec. is to apply to a non-trading corporation whose objects are confined to a single Part A or Part B State.

Other Cases of Alteration of Memo.: These are (i) under s. 94 with regard to the increase of the share capital of a Co., (ii) under s. 100 with regard to reduction of share capital, (iii) under s. 323 with regard to the alteration of the limited liability of directors to unlimited liability, (iv) under s. 393 on a scheme of arrangement.

ARTICLES OF ASSOCIATION

Articles of Association, their nature: The articles of association are the rules and regulations of a Co. framed for the purpose of managing its affairs. They are distinguished from Memorandum in this that whereas the latter defines and formulates the fundamental conditions of the Co.'s incorporation including the object or objects for which the Co. is formed, the former merely lay down the various means and methods which the Co. desires to adopt for fulfilling those conditions and for achieving those objects. As Bowen, L.J. put it in *Guinness v. Land Corporation of Ireland* (j), "the memorandum contains the fundamental conditions upon which alone the Co. is allowed to be incorporated. The articles are the internal regulations of the Co.". The articles generally provide for all matters of internal administration of the Co., e.g. the business of the Co., the amount of capital issued, the classes of shares into which it is divided and the rights of each of the respective classes, rules as to making of calls, as to the Co.'s lien, as to forfeiture of shares, transfer of shares, alteration of capital, holding of meetings, voting at meetings, quorum, rules as to the number and appointment of directors and their powers, as to declaration of dividends, as to keeping of register of members, as to accounts and audit, etc. Some articles contain provisions as to the increase and reduction of share capital and also lay down the borrowing powers of the Co. Articles may authorise the issue of redeemable preference shares, to consolidate shares into shares of larger amount, to convert paid-up shares into stock and to reconvert stock into paid-up shares, to sub-divide shares into shares of smaller amount, to cancel shares not taken up or agreed to be taken up, to reduce its share capital, to keep share premium account and a capital reserve fund. The articles may also authorise the Co. to alter its Memo. so as to impose unlimited liability on directors and officers. When share or stock warrants are intended to be issued, power to do so must be reserved in the articles.

Table A: It is not absolutely necessary for every limited Co. to have its own special articles. This is clear from the language of s. 26 which says that in case of a public Co. limited by shares, articles may (or may not) be registered with the Memo. In case of unlimited Co.s, Co.s limited by guarantee and private Co.s limited by shares, however, articles *must* be registered along with the Memo. Articles of a Co. limited by shares may adopt all or any of the regulations of Table A to Schedule I of the Act. Where a Co. registered after the commencement of the Act frames no special articles for itself however s. 28 provides that regulations in Table A in the first schedule to the Act, shall govern the internal administration of the Co.'s affairs. Even where articles are framed by a Co. the sec. provides that in so far as they do not exclude or modify the regulations in Table A, the latter shall, so far as applicable, be the regulations of the

company, "in the same manner and to the same extent, as if they were contained in duly registered articles". Table A here referred to, consists of a series of regulations, formulated by the legislature for the conduct of the affairs of a company and included in Schedule I to the Act, and the effect of these secs. is that these regulations, in so far as their operation is not excluded by the articles of a Co. will govern and regulate the internal management of the affairs of the Co. The binding effect of the provisions of Table A, thus laid down was sought to be further extended by Act 22 of 1936 (which amended the Act of 1913), by making certain regulations in Table A compulsorily applicable to all Co.s. These regulations have been now incorporated as secs. in the present Act and thus the cumbersomeness of the old drafting is avoided.

Form of Articles : It should be noted that Articles of association may adopt all or any of the regulations in Table A (s. 28) or may be entirely different, to suit the special needs of the Co. Under s. 27, however, in case of an unlimited Co., the articles shall state the number of members with which the Co. is to be registered, and if it has a share capital, the amount thereof. In the case of a guarantee Co., the articles shall state the number of members with which the Co. is to be registered. Notice in this connection that under s. 37, in case of a guarantee Co. registered on or after 1st April 1914 and not having a share capital, every provision in the Memo. or articles or in any resolution of the Co., purporting to give a person the right to participate in the profits of the company, otherwise than as a member, shall be void. This provision prevents any person from sharing in the profits of a guarantee Co. unless he is a member and as such, under a liability to contribute to its assets on a winding up. Further in case of Co.s above described, every provision in the Memo. or articles or resolution of the Co. purporting to divide the undertaking of the Co. into shares or interests shall be treated as a provision for share capital, though the nominal amount of the share or interest is not specified thereby. The sec. further provides that in the case of private Co.s having a share capital, the articles shall contain provisions: (i) restraining right to transfer shares, (ii) limiting number of such members to 50, and (iii) prohibiting invitation to the public to subscribe for shares. Where a private Co. has no share capital, only (i) and (ii) above, should be provided for. Articles of Co.s other than those having share capital, shall confirm, as far as possible, to the Forms in Tables C, D and E in Schedule I to the Act (s. 29). Articles must be printed, divided into consecutively numbered paras and must also be signed by each subscriber to the Memo., with his address, description and occupation added in the presence of one witness, who shall attest the same in the same manner (s. 39). Unsigned articles, however, if acted upon by members for a long period, will be binding on them, provided they have been registered (k). Where registration of articles is compulsory and the Co. has no special or separate articles, the usual procedure followed is to adopt Table A as the articles of the Co. and register the same along with the Memo.

Notice that articles must not contain provisions which are contrary to the Act, the provisions of the Memo. or which are otherwise illegal. Thus an article taking away a member's right to sue the Co. is void (l). So too, an article empowering the Co. to issue shares at a discount (otherwise than as provided by the Act) is void (m). An article taking away a member's right of inspection of the Co.'s documents has also been held to be void (n). An article taking away or restricting the right of members to alter the articles is also void. Where an article provided that a member whose name was not on the Register for a continuous period of two months immediately preceding the date of meeting, was not entitled to vote or be reckoned in a quorum, held, the article was invalid (o).

Registration of Articles and Memo. (s. 33): The Memo. and Articles (if any) must be presented to the Registrar of the State in which the registered office of the Co. is stated by the Memo. to be situate, for registration. Any agreement which the Co. proposes to enter into with any firm, individual or body corporate to appoint them Managing Agent or Secretaries and Treasurers of the Co., must also be presented to the

(k) *Tung v. Man Ins. Co.* (1902) A.C. 232.

(l) *Hope v. International Finance* (1876),

4 Ch. 327.

(m) *Walton v. Saffery* (1877) A.C. 299.

(n) *Re Houston Navigation Co.* (1912) W.N. 110.

(o) *Vishwanath v. Tiffins Barylls Asbestos etc. Ltd.* (1953), 1 Mad. L.J. 346.

said Registrar for registration, along with Memo. and articles. Further a declaration signed by an Advocate of the Supreme Court, an Attorney, a pleader (entitled to practise before the High Court), or a Chartered Accountant practising in India, or by any person mentioned in the articles as director, managing agent, manager, secretaries and treasurers or secretary of the Co., stating that all requirements of the Act and of the rules made thereunder regarding the registration and matters precedent and incidental thereto, have been duly complied with, shall also be filed with the Memo. and articles. The Registrar may accept such declaration as sufficient evidence of compliance. If the Registrar is satisfied that all the above requirements are fulfilled and that the Co. is authorised to be registered under the Act, he shall retain and register the Memo., articles and the aforesaid agreement (if any).

Effect of Registration : On the registration of the Memo. and the articles the Registrar shall certify under his hand that the Co. is incorporated and that it is a limited Co. (if it is such). This certificate is known as the "*Certificate of Incorporation*". From the date of incorporation mentioned in the "certificate", the subscribers to the Memo. and other persons who may become members of the Co. shall be a body corporate, by the name mentioned in the Memo., capable of exercising all functions of an incorporated Co. and having perpetual succession and a common seal. Their liability to contribute to the assets of the Co., however, shall be only what is laid down by the Act (s. 34). The duties of the Registrar with regard to registering a Memo. and/or articles under the above sec. are quasi-judicial as well as ministerial. He should not register a Memo. which does not comply with the provisions of the Act, e.g. where the objects are too vague or where one or more objects are illegal (p).

Certificate of Incorporation

As sec. 35 of the Act provides, a "certificate of incorporation" given by the Registrar in respect of any association shall be *conclusive evidence* that all the requirements of the Act in respect of registration and of matters precedent and incidental thereto have been complied with and that the association is a Co. authorised to be registered and duly registered under the Act. The certificate is, by the sec., made conclusive as to the question, whether all the necessary formalities prior to registration have been duly complied with. The reason for so holding was expressed by Lord Cairns in *Peel's Case* (q) as follows: "When once the memorandum is registered and the company is held out to the world as a company undertaking business, willing to receive shareholders and ready to contract engagements, then, it would be of the most disastrous consequences, if, after all that has been done, any person was allowed to go back and enter into an examination of the circumstances attending the original registration and the regularity of the execution of the documents". Thus where a Memo. was altered after subscription in such a way that the alteration "entirely annihilated" the original execution of the document, but the Registrar registered the Memo. without notice of the fraud and issued a "certificate of incorporation", it was held that the Co. was validly constituted and the original contract could not be set aside. The same result would follow, even if it subsequently turns out that all subscriptions were, in fact, made by one and the same person or were forged. Similarly, the certificate would preclude inquiry as to whether the subscribers or some of them were in fact minors (r). The certificate is also conclusive as to the day on which the Co. was registered and incorporated (s). The difficulty, however, is not without a remedy, and the opinion has been expressed that, in such a case, the Crown or the Attorney-General may move by way of "*certiorari*" to cancel the registration (t).

Consequences of Incorporation : One of the most important consequences of incorporation is that from thenceforth the Co. becomes a separate "*legal persona*" or entity, quite distinct from the shareholders composing it (u). Its property is not in the property of the shareholders, the right of any individual shareholder being only a right to have a share of the profits of the Co. when realised and divided. So also any liability

(p) *Ex parte More* (1931), 2 K.B. 197.
 (q) (1867), 2 Ch.App. 674.
 (r) *Moosa v. Ebrahim Gulam*, 14 Bom. L.R. 1211.
 (s) *Re Jubilee Cotton Mills* (1928), 1

Ch. 1.
 (t) *Bowman v. Secular Society* (1917) A.C. 406.
 (u) *Dhulia Amalner Transport Co. v. Raychand*, A.I.R. (1952) Bom. 337.

of the Co. is not the liability of the individual shareholders and a creditor of the Co. can only proceed against the Co. (v). The Co. can also sue in its corporate name and can hold and enjoy property in such name. A "legal person", however, is a mere abstraction of law (w). Thus a Co. cannot appear in a court of law in person. It must appear either by counsel or solicitor, where solicitor is allowed (x).

Memo. and Articles : Public Documents : It has been held in England that the Memo. and articles of a Co. on registration become public documents (y). This has important consequences, particularly as regards outsiders, who can always inspect these documents at the Registrar's office, and who, therefore, are fixed with notice of their contents (see seq.).

Articles of Association : their Legal Effect

As regards the legal effect of articles, s. 36 of the Act provides that subject to the provisions of the Act, the Memo. and articles shall, when registered, bind the Co. and the members thereof to the same extent as if they respectively had been signed by each member of the Co. and contained covenants on the part of each member of the Co. to observe all the provisions of the Memo. and the articles. The sec. further provides that all money payable by any member to a company under the Memo. or articles shall be a "debt" due from him to the Co. The effect of these provisions is to constitute the Memo. and articles of association of a Co., a contract between each member and the Co., the various cls. and regulations operating as so many "covenants" on the part of each member, his heirs and legal representatives and the Co. to observe the same. The provisions of the Memo. and articles, therefore, may be looked at in the following ways :

(i) as between the members and the Co., the Memo. and articles constitute covenants or contracts by which each member is bound, though no member has actually signed the same. As Ashbury J. said in *Hickman v. Kent and Romney Marsh Association* (z), "though the articles can neither constitute a contract between the Co. and an outsider nor can give any individual member special contractual rights beyond those of the members generally, yet they do in fact constitute a contract between a Co. and its members in respect of their ordinary rights as members". The learned Judge also stated that "general articles dealing with the rights of members as such should be treated as statutory agreement between them and the Co. as well as between themselves *inter se*". Thus where articles provided that the shares of any member who became bankrupt should be sold to certain other persons at a certain price, it was held that the trustee in bankruptcy of a member was bound by the terms and could not claim the shares against the company (a). Similarly, if articles validly give a lien to the Co. on the shares of members in certain cases, any person becoming a member of the Co. would be bound by the provisions, even though he was in fact ignorant of them when he bought the shares (b). (ii) The Co., too, is, as regards its members, bound by the provisions contained in the Memo. and articles, as on a covenant or contract. The Co., therefore, can exercise its rights, as against any member, only in pursuance of and in accordance with the articles and not further or otherwise. Thus a forfeiture of shares, irregularly effected by a Co., will be set aside at the instance of the member aggrieved (c). (iii) As between the members *inter se* also, the Memo. and articles are binding on each member as against the other or others, on the basis of an implied covenant or contract to be bound by the Memo. and articles (d). The rule with regard to their breach, however, has this peculiarity that where a member complains of a breach of any provisions of the articles by another member, the suit must be brought by the Co. itself, and not by the individual member whose rights are injured (e). (iv) As between the Co. and an outsider, however, the Memo. and articles are not binding on the Co., i.e. an outsider cannot take advantage of their provisions, to found a claim thereon against the Co. This is because the outsider is not a party to the contract and

(v) *Haribai v. Bansai*, 11 Pat. 174.

(w) *G.E. Rly. Turner* (1872) L.R. 8 Ch. App. 152.

(x) *Tritonia Ltd. v. Equity Law and Fire Ins. Co.* (1943) A.C. 584.

(y) *Credit Bank's case* (1926), 2 K.B. 450.

(z) (1915) 1 Ch. 881.

(a) *Borland v. Steel Bros.* (1902), 1 Ch.

279.

(b) *Bradford Banking Corp. v. Briggs*, 12 A.C. 29.

(c) *Johnson v. Little's Iron Agency* (1877) 5 Ch.D. 687.

(d) *Wood v. Odessa Water Works Co.*, 42 Ch.D. 636.

(e) *Foss v. Harbottle* (1843), 2 Hare 461.

therefore cannot sue on it. Thus a provision in the articles to pay remuneration to the promoters, constitutes no contract between them and the Co. on which they can sue the Co. in damages, if the remuneration is not paid to them (f). Similarly, where a Co., by its articles, provided to employ E but did not employ him, it was held that E could not recover any damages against the Co. (g). It would be otherwise, however, where the articles or some of them have been, by implication, incorporated in a contract with an outsider.

S. 36 further provides that the liability of the members for all moneys payable under the Memo. or articles shall be a "debt" due by the member to the Co. Though this is undoubtedly so, it is to be observed that the liability is not enforceable against a member until a valid call has been made under the articles. Thus, a mortgagee purchaser of the rights of a company, cannot enforce by suit, the liability of shareholders for the amounts unpaid on their shares, and a mere demand by him as auction purchaser cannot take the place of a valid call (h).

Articles and Memorandum: their relation: As pointed out in *Guinness v. Land Corp.* (i) articles are subject to the Memo. and cannot give powers which are not conferred by the Memo. nor can they purport to create rights which are inconsistent with the Memo. The rule with regard to this may be stated as follows: (i) with regard to matters which must, by statute, be provided by the Memo., the latter must be regarded as the dominant document (j). (ii) Except as above, however, the Memo. must not be regarded as the dominant document but must be read in conjunction with the articles which may be used to explain or amplify the Memo (k). This is because the two are contemporaneous documents, registered at the same time and therefore if there is any ambiguity or if the Memo. is silent on any point, the articles may serve to explain or supplement the Memo. (iii) Where, however, there is no ambiguity or lacuna in the Memo. its terms cannot be controlled or modified by the provisions of the articles. Thus, where the directors of a Co. in the exercise of the absolute discretion given to them by the articles, attempted to use a reserve fund, specially created by the Memo., for the benefit of the preference shareholders, for other purposes, it was held that it could not be done (kl).

Alteration of Articles

As s. 31 provides (i) subject to the provisions of the Act and (ii) the conditions contained in the memorandum, a company may (iii) by *special resolution* alter or add to its articles and such alteration or addition, so made, shall be valid as if originally contained in the articles and shall be subject to alteration in a like manner by special resolution.

The sec. gives an almost unlimited power to a Co. to alter its articles and where the alteration is properly made a shareholder will not be heard to say that he is not bound by the altered articles. The reason is that the shareholder must be deemed to know that one of the incidents of membership in a Co. is that the Co. may, by adopting the proper method, alter its articles. This right of alteration of articles, however, is *subject to certain conditions*: (i) the alteration must not be inconsistent with or go beyond the provisions of the Memo. If it does, it will be "ultra vires" and wholly void and inoperative; (ii) it must not purport to sanction anything which is illegal or opposed to the provisions of the Act (k2); (iii) it must be made by means of a special resolution as defined by the Act. Certain other conditions have also been added to the above, by judicial decisions, viz. (iv) the power of alteration should be exercised *bona fide* for the benefit of the company as a whole and (v) not oppressively or in fraud of the minority. (vi) Under s. 38 no member of a Co. is bound by any alteration of the Memo. or articles, after the date he became a member, the result of which is to require him to take or subscribe for more shares or which otherwise increases his liability in

(f) *Re Ratherham Alum and Co.*, 25 Ch. D. 103.

(g) *Eley v. Positive etc. Co.* (1876), 1 Ex. D. 88.

(h) *Pubna Dhan Bhandar Co. v. Fayezuddin*, 59 Cal. 1186; *Vishwanath v. Holland Cinetone Ltd.* (1939) A.L.J. 950.

(i) (1882), 22 Ch. 349.

(j) *Harrison v. Mexican Rly. Co.* (1875) L.R. 10 Eq. 358.

(k) *Anderson's case* (1877), 7 Ch.D. 75.

(kl) *Angostura Bitters Ltd. v. Kerr* (1933) A.C. 550.

(k2) *Menier v. Hooper's Telegraph Co.* (1874) L.R. 9 Ch.App. 350.

respect of shares held by him at the date of the alteration, except with his written consent, whether obtained before or after the alteration. The result of the last condition is to put a stop to the undesirable practice of directors and others, who by alteration of articles, indirectly compel members to increase their holdings in the Co. or increase their liability to the Co. against their will.

Can articles be amended if the alteration involves breach of contract with a third person? It has been held that a Co. cannot be precluded from altering its articles, thereby giving itself powers to act according to the altered articles, though this may involve a breach of a contract with another person. *Southern Foundaries Ltd. v. Shirlow* (k3). In this case a Co. called S. Ltd. had, by an agreement dated 21-12-33, appointed one Shirlow, who was already a director, as a managing director of the Co. for a period of 10 years. While the contract had still 7 years to run, another Co. called F. Ltd. acquired all the shares of S. Ltd. By a special resolution passed in April 1936 the existing articles of S. Ltd. were abrogated and new articles were adopted. The new articles empowered F. Ltd., by an instrument subscribed by two directors, and the secretary, to remove any director of the Co. In March 1937 F. Ltd. purported to exercise the power and dismissed Shirlow from his office as director and S. Ltd. thereupon treated him as having ceased to be a managing director. *Held*, by the House of Lords (by majority), in a suit by Shirlow against S. Ltd. for breach of contract and against F. Ltd. for procuring the breach, that under the circumstances, although the alteration of the articles by S. Ltd. did not amount to a breach of contract,—every company having an inherent right to alter its articles—still the removal of Shirlow from his office as managing director before the lapse of the agreed period was a breach of contract on the part of S. Ltd. and that it was not the less so, because it required two acts and not one only for its accomplishment. Both the companies were therefore held liable to Shirlow in damages.

The alteration can only be made by a special resolution as provided by the sec. and not by an ordinary resolution, even though the articles themselves lay down the latter procedure. This was attempted to be done in *Navanital v. Scindhia Steam Navigation Co.* (l), where the qualification of directors was sought to be raised, by a resolution passed at a general meeting, from Rs. 30,000 worth of shares to Rs. 75,000 worth of shares. *Held*, the resolution was “*ultra vires*” and illegal. The court also doubted, whether an article allowing such a thing to be done by ordinary resolution would be legal. It has been held that articles can be treated as altered by reason of continued acquiescence of the shareholders in the alteration, as shown by a long course of dealings (m). Articles when altered, take effect and are valid, as if the alteration was originally contained in the articles. This gives retrospective effect to the alteration, but it is permitted by the Act (n). (See s. 31 of the Act.)

Member's right to copy of Memo. and articles: A Co. is bound within 7 days on a request in that behalf, from any member and on payment of a fee not exceeding Re. 1 to furnish to such member, a copy of (i) the Memo., (ii) the articles, and (iii) any agreement entered into or proposed to be entered into with any person, appointed or to be appointed managing agents, secretaries and treasurers, and (iv) of every agreement and every resolution referred to in s. 191 which have not been incorporated in the Memo. or articles. In case of default, the Co. and every officer who is in default shall be liable to a fine (upto Rs. 50) for every offence (s. 39).

Procedure on alteration of articles or Memo.: Where an alteration is made in the articles or Memo. or in agreement referred to in cl. (iii) of s. 39 (see above), or in any other agreement referred to in s. 192, every copy of the Memo. or articles which is subsequently issued must be in accordance with the alteration. If a Co. issues any copies of the Memo. or articles, which are not in accordance with the alteration, the company shall be liable to a fine of Rs. 10 for each such copy and every officer of the company, who is in default, shall also be liable to a like penalty (s. 40).

Registration of Unlimited Company as Limited: Under s. 21 a Co. registered as unlimited under the Act may register itself under this Act as a limited Co., and similarly

(k3) (1940) A.C. 701.

(l) 22 Bom. L.R. 1362.

(m) *Ho Tung v. Man of Ins. Co.* (1902)

A.C. 232.

(n) *Andrews v. Gold Reefs etc. Ltd.*

(1900), 1 Ch. 656.

a Co. already registered as a limited Co. may re-register itself as a limited Co. On such registration or re-registration, the Registrar shall close the former registration. The fresh registration or re-registration shall be made in the same manner and shall have the same effect as if it were the first registration of the Co., except that the Registrar may dispense with delivery to himself of documents which are already in his possession. Such registration or re-registration of an unlimited Co. as limited shall not affect any debts, liabilities, obligations or contracts, incurred or entered into by or on behalf of the Co., before registration, and the same may be enforced against the Co. as provided in Part IX of the Act, with regard to Co. registered thereunder. All property belonging to the Co. at the date of registration will vest in the Co. after incorporation. Registration does not affect the rights or liabilities of the Co. in respect of any debt or obligation incurred before registration. All actions and other legal proceedings pending by or against the Co. before registration may also be continued against the Co. after registration.

"Member" of Company

A person can become a "member" of a Co. in any of the following ways: under sec. 41, (i) subscribers to the Memo. of a Co., shall be deemed to have agreed to become members of the Co. and on the registration of the Memo. shall be entered as members in the Co.'s Register of members; (ii) every other person who (a) agrees to become a member of the Co. and (b) whose name is entered on the Register shall be member of the Co. (iii) A person can also become a "member" by the transfer of a share to him or (iv) by devolution, on death or otherwise of an existing member, or (v) by "transmission", e.g. where articles provide for transmission of shares held by one in favour of another on the happening of a certain contingency and lastly, (vi) by an order or decree of a Court of Law. Notice however that under s. 42, a body corporate cannot be a member of its holding Co. and an allotment or transfer of its shares by holding Co. to its subsidiary is void. Only in the following cases is such membership allowed, e.g. (i) where the subsidiary concerned is the legal representative of a deceased member of the holding company, and (ii) where the subsidiary concerned is a trustee (unless the holding Co. or a subsidiary thereof is beneficially interested in the trust), and is not so interested only by way of security for an ordinary business transaction including the lending of money. In other words, as a general rule, no subsidiary can be a member of its holding company or its subsidiary. It can be such member only as the legal representative of a deceased member of the holding Co. or as trustee for another person or persons. In the last case, however, the beneficial interest under the trust should not belong to the holding Co. The fact that the beneficial interest belongs to the holding Co., in virtue of an ordinary commercial transaction with subsidiary including lending of money (e.g. by way of mortgage), will not make the membership of the subsidiary Co. in its holding Co. invalid (cl. 2). The sec. further provides that where a subsidiary was a member of its holding Co. at the commencement of the Act or before becoming its subsidiary, it may continue to be such but the subsidiary shall have no right of vote at meetings of the holding Co. or of any class of members thereof (cl. 3), except in cases mentioned in exceptions (i) and (ii) above. The subsidiary may be member of its holding Co. by means of a nominee. The above provisions apply to such nominee also (cl. 4). Where the holding Co. is a guarantee or unlimited Co., reference to "shares" in the above sec. includes the interest of the members, whatever the form of that interest, and whether the Co. has a share capital or not (cl. 5).

Change in membership of private Company: Sec. 43 provides that when a private Co. ceases to conform to the statutory requirements as laid down in s. 3(1)(iii) of the Act (i.e. if its membership exceeds 50, it permits free transfer of shares or asks for public subscriptions), then, (i) it shall cease to enjoy the privileges conferred on private companies by the Act and (ii) shall be subject to all duties and obligations imposed by the Act on public companies. The Court however if it thinks just and equitable to grant relief (i.e. if default was due to inadvertence or accident or some other sufficient cause), may, on terms, order the Co. to be relieved from the above consequences, on the application of the Co. or any interested person. S. 44 further provides that where a private Co. by reason of alteration of its articles, ceases to conform to the requirements of s. 3(1)(iii), it shall cease to be a private Co. from the date of the alteration.

(iv) Within 14 days of the above date it shall file with the Registrar in the prescribed form a "prospectus" or "statement in lieu of prospectus". The prospectus shall state matters and set out reports mentioned respectively in Parts I, II and III, Sch. II, of the Act (see seq.). The "statement in lieu of prospectus", shall be in the form and contain particulars and reports mentioned in Parts I, II and III respectively of Sch. IV of the Act (see seq.). Where adjustments under cl. 32 of Sch. II or cl. 5 of Sch. IV are indicated in the "prospectus" or "statement in lieu of prospectus", a written statement signed by the person concerned and giving reasons therefor shall also be endorsed on the "prospectus" or "statement". If default is made in regard to the above matters, the Co. and every officer in default is liable to a fine (upto Rs. 500). If an "untrue statement" is included in a "prospectus" or "statement" filed under the sec., any person who authorised the same will be liable to imprisonment (upto 2 years) or fine (upto Rs. 5,000) or both, unless he proves that the untrue statement was immaterial, or that upto the time the "prospectus" or "statement" came to be filed he had reasonable ground to believe and did upto the time of filing the same, believe, that the statement was true. In the above connection, a statement is "untrue", if it is misleading in the form and the context in which it is included. An omission from the "prospectus" or "statement" of what is statutorily required to be contained therein, may amount to an "untrue statement". A statement or omission shall be deemed to be included if the statement or omission is contained in any report or memorandum appearing on the face of the above two documents or by reference incorporated therein.

Reduction of members below legal minimum: Under sec. 45, if at any time the number of members of a public Co. falls below seven and of a private Co. falls below two and the Co. carries on business for more than 6 months thereafter, the following consequences shall ensue: (i) every person who was a member of the Co. after those six months with knowledge of the above reduction, shall be severally liable for the whole debts of the Co. contracted during that time, and (ii) he shall be liable to be severally sued therefor.

CONTRACTS OF COMPANIES

Contracts of Companies: Various kinds of contracts are met with in Company Law with regard to Co.s: One class is the class of contracts which are entered into by a Co., in the ordinary course of its business. Another kind of contract is called the "*Preliminary Contract*", which has a special significance with regard to Co.s. The former class is treated below. The latter is dealt with later (see seq.).

Form of Contracts, Bills of Exchange and Pro-Notes executed by Co.: Ss. 46-48 lay down the following rules as regards the above: (i) a contract which by law is required to be made in writing, if between private persons, shall be made in the same way in case of a Co. and shall be signed by any person acting under the Co.'s express or implied authority in that behalf. It can be discharged or altered in the same manner also. (ii) Where a contract can, by law, be made between private persons by parole only and not reduced to writing, it can be made in the same manner in the case of a Co. and can be varied or discharged in the same manner. Such contracts shall be binding on the Co. (s. 46). (iii) A promissory note, bill of exchange or hundi shall be deemed to have been made, accepted, drawn or endorsed on behalf of a Co. if it is drawn, accepted, made or endorsed in the name of or on behalf of or on account of the Co., by any person acting under its express or implied authority in that behalf (s. 47). (iv) A Co. may, by writing, under its common seal, empower any person either generally or with regard to specific matters, as its attorney to execute any deed on its behalf, either in India or outside. A deed signed by such attorney and sealed by him (where sealing is required) shall be binding on the Co. as if executed under its common seal (s. 48). (v) A Co. whose business comprises transactions outside India, may, if authorised by its articles, have for use at such places, an official seal which shall be the facsimile of the common seal of the Co., with the name of such foreign place added. The Co. may, by a writing under its common seal, authorise any person to put such official seal on any document to which the Co. is a party at such place. Such agent's authority to execute documents under such seal, shall continue till the period mentioned in the writing expires or till notice of revocation is received by person dealing with such agent. The Agent must certify under his hand, the date and place at which the

document on which he puts such seal is executed. Such document shall be binding on the Co. (s. 50).

Three rules may be observed with regard to contracts by Co.s: (i) a contract "ultra vires" the Co. is wholly void and cannot be enforced or ratified. (ii) A contract not "ultra vires" the Co. but "ultra vires" the directors, can be ratified by the shareholders. (iii) A contract entered into before the incorporation of the Co. by some person professing to act on its behalf, cannot be ratified by the Co. But there is nothing to prevent a Co. from entering into a new contract to carry into effect the terms of the pre-incorporation contract. To these rules the Legislature has added a fourth, viz. (iv) a Co. cannot enter into a binding contract till it is entitled "to commence business" (see s. 149).

It is often difficult to decide, when a bill of exchange or pro-note is signed by A as the director or manager of a Co. whether in such a case, either the Co., the director, or manager or both are liable. As was stated by Rankin, C.J. in a Calcutta case, "the question of the liability of the Co., on a particular endorsement is in every case a question of construction. If on the true construction of the instrument, the bill or note is the bill or note of the Co., the Co. will be liable upon it, not the individuals whose names are upon it, unless the bill or note is the bill or note of both. On the other hand, if on a true construction of a bill or note, it is not the bill or note of the Co., the persons whose names are upon it will be liable, whether they intended to do so or not". Where, therefore, the endorsement was "M. and Sons, Managing agents of L.A. & Co.", it was held that it would not be necessarily clear to anyone that the responsibility of L.A. & Co. was involved and that therefore L.A. & Co. were not liable on the bills (o). In the same way, when a hundi drawn on A, was accepted by A "for and on behalf of B & Co.", it was held that there was no valid acceptance by A, to justify a suit against A, as distinguished from the Co. (p). In a Bombay case, one of the agents, secretaries and treasurers of a Co. had signed a pro-note, in his own hand, to pay for the price of machinery purchased by the Co. The note was written on a form of letter paper of the Co. and bore a rubber stamp impression of the name of the Co. In a suit on the pro-note against the Co., held, the Co. was liable because there was no doubt that the note was signed on behalf of the Co., which had purchased the machinery (q).

Contracts by agents of Company: S. 416 lays down a special rule with regard to contracts entered into on behalf of a public Co. (or its subsidiary private Co.) by managing agent, secretaries and treasurers, manager or other agent, in which the Co. is an undisclosed principal. They are required to make a memo. of the terms of the contract at the time, specifying the person with whom it is entered into. The memo. must be forthwith filed with the Co. and copies thereof must be sent to each director. The memo. should also be placed before the Board at its next following meeting. In case of default, the contract is voidable at the option of the Co. against the Co.; the person entering into such a contract and every officer in default are also liable to a penalty.

Investments of Company

Under sec. 49, all investments made or held by a Co. shall be registered or held by the Co. in its own name. Where, at the commencement of the Act, it is otherwise, the Co. shall comply with the above requisition within one year of the commencement of the Act or dispose them off. Where however the Co. has the right to appoint director or directors in another Co. or where a nominee of the Co. has been so appointed, shares of the latter Co. not exceeding the amount of qualification shares for such director or directors, may be registered or held by the Co. jointly in the name of itself and each of such persons or nominee, or in the name of each such person or nominee expressly described as such. Further a Co. may hold shares in its subsidiary in the name of its nominee or nominees, so far as to ensure that the number of members of such subsidiary is not reduced below 7 in case of public and below 2 in case of private subsidiary. The sec. also does not apply to a Co. whose principal business consists of buying

(o) *Shreeclal v. Lister Antiseptic etc.*, 52 Cal. 802.

(p) *Ibrahim Fazalbai v. International*

Banking Corp., 27 Bom. L.R. 283.

(q) *Poona Chitrashala Press v. Gajanan*, 24 Bom. L.R. 355.

and selling shares or other securities. The sec. does not prevent a Co. from depositing with its bankers, shares and securities held by it for collection of interest or dividend. A Co. can also deposit with or transfer to any person, shares or securities held by it as security for repayment of a loan or performance of any obligation. Where shares and securities constituting its investments, are not held as permitted in the abovementioned cases, in its own name, the company shall forthwith enter in a register to be kept for the purpose, the nature, value and all other necessary particulars with regard to them and also the name of the Bank or person in whose name or custody such shares and securities are held. Such register shall be open to inspection of every member and debenture-holder of the Co., during business hours (not being less than 2 hours each day) subject to reasonable restrictions. If inspection is refused the Court may order immediate inspection. Certificates of and letters of allotment regarding shares and securities held by the Co. in its own name must be kept by the Co. in its own custody or in the custody of its Bank (being a scheduled Bank). Punishment for default in complying with any of the above requirements, by the Co. or any officer thereof is a fine (upto Rs. 5,000). This sec. is entirely new. The sec. does not apply to investment Co. whose business consists of buying and selling of shares, stocks and debentures and other securities.

PROSPECTUS AND PROMOTERS

Prospectus: its nature: As will be observed, a "prospectus" is defined by s. 2, cl. 36, of the Act, as "any prospectus, notice, circular, advertisement or other invitation, offering to the public for subscription or purchase, any shares or debentures of a body corporate". A prospectus is a circular issued by a promoter of a Co. or by the directors of a Co. to induce the public to subscribe for shares of the Co. It is thus a formal document which must contain the particulars as set out in s. 56 before it can be placed before the public. The omission to set out any of the said particulars is heavily penalised. The reason for the stringent rule is that a prospectus is, in effect, an invitation to the public to contribute their capital in a proposed corporate enterprise, and inasmuch as those who are behind the proposed Co. have all the knowledge or means of knowledge as to the future prospects and present situation of the proposed enterprise and the investing public has none, it is but right that the former should not only disclose all the matters within their knowledge, relating to the proposed enterprise, which might affect the investing mind but should state them accurately, correctly and unambiguously. As Kindersely, V.C. stated in *New Brunswick and Canada Rly. Co. v. Muggeridge* (r), "those who issue a prospectus, holding out to the public great advantages which will accrue to persons who take up shares on the representations therein contained, are bound to state everything with scrupulous accuracy and not only to abstain from stating as facts, that which is not so, but to omit no fact, within their knowledge, the existence of which might in any degree affect the nature or extent or quality of the privileges and advantages, which the prospectus holds out as inducement to take shares."

It is not necessary that every Co. should issue a prospectus. But, where a Co., on its formation, does not issue a prospectus, it is obliged, under s. 70 to prepare and file with the Registrar, what is called a "*statement in lieu of prospectus*" (see seq.) which is analogous to a prospectus, though it is framed on a smaller scale. A prospectus may be issued, not only where shares are to be offered for public subscription, but also where a Co. wants to raise money by issue of debentures to the public. In both cases, however, the legal requirements and obligations are the same. The legal importance of a prospectus lies in this that it contains the terms and conditions under which a prospective shareholder buys the shares. The question whether a particular document issued by a Co. is a "prospectus" within the meaning of the above sec. is one of construction. In *Nash v. Lynde* (s), two documents were issued for circulation among directors and their friends and a letter marked private and confidential, written on company's paper with names of directors appearing thereon, sent to a co-director. Plaintiff had purchased shares on the footing of these documents which he obtained from a friend of a director. He sued in damages for failure to state in the documents the number of shares issued within past two years as paid for otherwise than in cash. *Held*, the documents were not issued to him as an invitation to subscribe for the shares

but in order to give him a general idea of the position of the company and were, therefore, not "prospectuses" and the action failed. Where shares are alleged to have been bought on the faith of a "prospectus", two questions arise for consideration, (i) was there a "prospectus" and (ii) was it "issued"? To be a "prospectus", the document must contain an "offer" to the public for subscription. An invitation, only intended for a single individual, will not be a "prospectus". If, however, the words of the document clearly show the intention to offer to the public, it would certainly be a "prospectus". The next question is, was it issued? As Lord Atkins pointed out in *Lynde v. Nash* (t), there are no words in s. 81 of the English Act of 1908 (corresponding to s. 56 of the present Indian Act), like "issued to the public". If, therefore, a prospectus is delivered to a person in whose hands it would serve the purpose of inviting anyone who may desire to subscribe, it will be deemed to have been "issued". Thus if an offer is sent solely to the shareholders and debenture-holders of a company it cannot be said to be made to the public. On the other hand, an offer is made to the public when over and above these parties, it is made to other parties as well (u). Similarly when some directors without the authority of the Co. sent a prospectus marked "not for publication" to their personal friends, it was held that the prospectus was not "issued" (v). In this connection, the provisions of s. 67 of the Act may be considered. Under the sec., (a) subject to any provisions in the Articles, "offering shares or debentures to the public" shall include offering them to any section of the public (whether selected as existing members or debenture-holders of the company or as clients of the person issuing the prospectus or otherwise). (b) Similarly, invitation to the public to subscribe for shares or debentures of a company, shall, subject as above, include an invitation to any section of the public (selected as above or otherwise). (c) No offer or invitation, however, shall be construed as being made to the public if (i) the same is not calculated, directly or indirectly, in the shares and debentures becoming available for subscription or purchase by persons other than those receiving the same or (ii) if it appears to be a domestic concern of the person making and receiving the offer or invitation; (d) a provision in the articles prohibiting offer of share or debentures to the public shall not be deemed to be infringed by an offer or invitation falling under (c) above. (e) Provisions of the Act relating to private companies shall also be similarly construed. Marking the prospectus as "confidential" or "for private circulation only" will not make it the less an invitation to the public if it is such otherwise (w).

Contents of Prospectus: The contents of a prospectus are now statuted. Under s. 55 every prospectus issued by or on behalf of a Co. or intended Co. or by or on behalf of any person who is or has been engaged or interested in the formation of a Co. shall be (i) dated and the date shall be deemed to be the date of its issue; (ii) it should also state the matters stated in Part I of Schedule II of the Act and (iii) set out the Reports set out in Part II of Schedule II of the Act. The matters so stated and the Reports so set out, shall have effect, subject to the provisions of Part III of the said Schedule.

The combined effect of the above provisions is as set out below: Every prospectus issued as above shall be dated and shall state (i) the main objects of the Co., with the names, occupations and addresses of the signatories to the Memo. and the number of shares subscribed by them; (ii) the number and classes of shares and the nature and extent of the rights of the holders thereof in the property and profits of the Co.; (iii) number of redeemable shares intended to be issued, the date of their redemption, if no date is fixed, the period of notice required for redeeming, with the proposed method of redemption; (iv) number of qualification shares fixed for directors; (v) provision in articles for remuneration of directors for services rendered to company as directors, managing director or otherwise; (vi) names, occupations, and addresses of director or proposed director, managing director or proposed managing director, managing agent or proposed managing agent (if any), secretaries and treasurers (if any) and manager or proposed manager (if any); (vii) any provision in the articles or in any contract, as to the appointment of managing director, managing agent, secretaries and treasurers, or manager; the remuneration payable to them and compensation (if any) payable to them

(t) (1928), 2 K.B. 93.

(u) *Burrows v. Malabele Gold Reef etc. Co.* (1901), 2 Ch. 23.

(v) *Sherwell v. Combined Incandescent Synd* (1907) W.N. 110.

(w) *Re South of England Gas Co.* (1911), 1 Ch. 573.

for loss of office; (viii) where company is managed by managing agents or secretaries and treasurers, who are a corporate body, the subscribed capital of that body; (ix) where shares are offered to the public for subscription, the minimum amount in the opinion of the directors or the other signatories to the Memo., after due inquiry, which will be required to be raised by such issue for each of the following purposes (distinguishing the amount under each head): (a) purchase price of any property purchased or to be purchased out of the proceeds of the issue; (b) preliminary expenses payable by the Co., including commission payable to any person for subscribing or agreeing to subscribe or for procuring or agreeing to procure subscription for shares of the Co.; (c) repayment of moneys borrowed for the above purposes; (d) working capital; (e) any other expenditure stating its nature, purpose and estimated amount; (x) the time of opening the subscription list; (xi) amount payable on application and allotment of each share; in case of a second or subsequent offer, the amount offered for subscription on each previous allotment within two preceding years; the amount actually allotted and amount paid on such allotment; (xii) substance of any contract or arrangement, effected or proposed, giving or proposing to give, any option or any preferential right to any person, to subscribe for shares in or debentures of a Co. with the following particulars: (a) number, description and amount of the shares or debentures, (b) the period during which the option or right is exercisable, (c) the price payable for the shares and debentures under the option or right, (d) the consideration (if any) for giving such option or right, (e) names, description and addresses of the persons to whom such option or right or rights thereto, are given or proposed to be given, and if to existing shareholders or debenture-holders, description and number of the relevant shares and debentures, (f) any other material facts relevant to the giving of the option or right of rights thereto; (xiii) number, description and amount of shares and debentures which within 2 preceding years have been issued or agreed to be issued as fully or partly paid up otherwise than for cash, the extent of such paying up and the consideration therefor; (xiv) the amount paid or payable by way of premium (if any) on each share issued or to be issued within 2 preceding years, stating dates or proposed dates of issue; and where some shares are issued or to be issued at a lower premium or at par or at a discount, the reasons for the differentiation, and how the premiums have been or are to be disposed of; (xv) where issue of shares or debentures is underwritten, the names of the underwriters, and the opinion of the directors that the latter are able to discharge their obligations; (xvi) where property is or is to be purchased or acquired or sub-purchased by the Co., which is to be paid for wholly or partly out of the proceeds of the issue in question and where purchase or acquisition of such property has not been completed at the date of the issue of the prospectus,—the names, description and addresses of the *vendors*, the amount payable or paid in cash, shares or debentures, to each of them separately, and specifying separately the amount (if any) paid or payable for goodwill, the nature of the title or interest in the property acquired or to be acquired, and short particulars of every transaction relating to the property in question completed within preceding 2 years, in which any vendor or any promoter, director or proposed director, had an interest, direct or indirect, specifying the date of the transaction, the name of the concerned person, and the amount payable to or by such person in respect thereof. The above does not apply to property, contract for the purchase of which was entered into by the Co. in the ordinary course of its business, and not in contemplation of the issue in question. It also does not apply to property in respect of which the purchase amount is not material. Where the vendor is a firm, it shall count as one vendor. “*Vendor*” includes every person who has entered into any contract, absolute or conditional, for the sale or purchase or for any option of purchase of any property to be acquired by the Co. where either (a) the purchase money has not been fully paid at the date of the issue of the prospectus, or (b) where the purchase money is to be paid wholly or partly out of the proceeds of the proposed issue or (c) where the contract depends for its validity or fulfilment on the result of the issue. Where the property is a leasehold, “*vendor*” includes the “*lessor*”, “*purchase money*” includes consideration for the lease and “*sub-purchaser*” includes a “*sub-lessee*”. (xvii) Consideration (if any) with its amount, nature and extent paid within 2 preceding years or agreed to be paid to any person or persons as commission, for subscribing or agreeing to subscribe or for procuring or agreeing to procure subscription for any shares or debentures of the Co. together with the name, description, address and occupation of each, the amount underwritten or sub-underwritten by each, the rate of commission payable

and any other material term or condition of such underwriting or sub-underwriting contract. The provisions as to sub-underwriter apply only in case he is a promoter or officer of the Co.; (xviii) amount or estimated amount of preliminary expenses and expenses of the issue, and the person to whom they are paid or are payable (not necessary where prospectus is issued more than 2 years after the Co. is entitled to commence business); (xix) any amount or benefit paid or given within preceding 2 years or intended to be given or paid to any promoter or officer and the consideration for the same; (xx) dates, parties and general nature of (a) every contract appointing or fixing remuneration of managing director, managing agent, secretaries and treasurers or manager, entered into any time, whether within or beyond preceding 2 years; (b) every other material contract, not being ordinary business contract or entered into more than 2 years before issue of the prospectus; (c) a reasonable time and place at which such contract or its copy can be inspected; (xxi) names, and addresses of the auditors if any; (xxii) full particulars of the nature and extent of the interest, if any, of every director or promoter (a) in the promotion of the Co. and (b) in any property acquired by the Co. within 2 years of the issue of the prospectus or to be acquired. Where such interest consists in being member of a firm or Co., the nature and extent of the interest of such firm or Co. together with statement of all sums paid or agreed to be paid to him, his firm or Co., in cash, shares or otherwise, by any person, to induce him to become or to qualify him as a director or otherwise for services rendered by him, his firm or Co. in connection with the promotion or formation of the Co.; (xxiii) where the capital is divided into different classes of shares, the voting rights at meetings of the Co. and the rights in respect of capital and income attached to each class of shares; (xxiv) where articles impose restrictions on the members' right to attend, speak or vote at meetings of the Co., or on their right to transfer shares or on directors, as to their rights of management, full particulars thereof; (xxv) if the Co. has been carrying on business, the length of time it has done so; (xxvi) if the Co. proposes to acquire any business, the length of time it has been carried on; (xxvii) if any reserves or profits of the Co. or its subsidiary have been capitalised, particulars of the same; (xxviii) surplus arising during preceding two years on any revaluation of the assets of the Co. or its subsidiary. The following reports shall be attached to the prospectus:—

(1) A report of the auditors of the Co. as regards: (i) profits and losses and assets and liabilities made up in the manner following, and (ii) the rates of dividends (if any) paid by the Co. in respect of each class of shares, for each of the five financial years immediately preceding the issue of the prospectus, and where no dividends have been paid for any class of shareholders during the above period, particulars of such class; (iii) if no account has been made up for any part of the five years period, ending three months before issue of the prospectus, a statement to that effect.

The auditor's report as regards (i) above, shall, *as regards profits and loss*, where the Co. has no subsidiaries, deal with to the profits and losses of the Co. (distinguishing non-recurring items) for each of the preceding 5 financial years and shall deal with the assets and liabilities of the Co. as at the last date on which the accounts are made up. Where the Co. has subsidiaries, the auditor's report either shall: (i) deal with the Co.'s profits and loss account separately as above, and further shall deal with the profit and loss account of each subsidiary or of all subsidiaries together so far as they concern the members of the Co., or (ii) deal with the whole profits and loss of the Co. including the profits and loss of all the subsidiaries together, so far as they concern the members of the Co.

As regards *assets and liabilities*: the auditor's report shall either (i) deal with the assets and liabilities of the Co. separately as above and further deal with the whole combined assets and liabilities of all the subsidiaries or deal individually with the assets and liabilities of each subsidiary, and in both cases, indicate the allowance to be made for persons other than members of the Co. as regards the assets and liabilities of the subsidiaries.

(2) If the proceeds or any part of the proceeds of the issue of shares or debentures are or is to be applied, directly or indirectly, in the purchase of a business, or an interest therein (exceeding 50% in the capital or profit and loss thereof or both), the prospectus shall have annexed thereto the report of accountants (to be named in the prospectus)

(i) of the profits and losses of the business for the immediately preceding five financial years and (ii) of the assets and liabilities of the business made up to not more than 120 days before the issue of the prospectus.

(3) If the proceeds or any part of the proceeds of the issue of shares or debentures are or is to be applied, directly or indirectly, in acquiring shares in another body corporate, and if by reason thereof, such body corporate becomes a subsidiary of the Co., the prospectus shall have annexed thereto, a Report of accountants (to be named in the prospectus), upon the profits and losses of the body corporate for the immediately preceding five financial years and upon the assets and liabilities of such body as of the last date on which its accounts are made up. The Report shall indicate how the profits and losses of the subsidiary as above would affect the members of the Co. and what allowance would have had to be made as regards assets and liabilities for holders of the remaining shares, of the subsidiary, if the Co. had at all material times held the shares to be acquired as aforesaid. If the subsidiary has sub-subsidiaries, the Report shall deal with the profits and loss thereof and the assets and liabilities thereof as stated in (1) above. The Reports mentioned above shall indicate by way of note, when necessary, any adjustment made as regards figures of profits and loss and assets and liabilities and state the fact of such adjustment having been made.

Further, where a Co. has been carrying on business or where a business has been carried on, for less than five financial years, the reference to "five financial years" in the above Reports shall be substituted by the period for which the Co.'s business accounts are made up. "Financial year" here means the period, whether greater or less than a year, for which a Co.'s or a business' accounts are made up (see Schedule II, Part III).

The Reports mentioned above are to be made by accountants qualified to act as auditors under the Act. Such accountants shall not be officers, servants or partners of or in employment of an officer or servant of the Co., or its subsidiary or holding Co. or subsidiary of the Co.'s holding Co. Notice that "Officer" here includes a proposed director but *not an auditor*.

Notice that as clause (2) of s. 56 provides, a condition requiring or binding the applicant for shares or debentures of a Co. to waive compliance with any of the requirements of the sec. or purporting to affect him with notice of any contract, document or matter not specifically referred to in the prospectus is void. Further, the provisions as regards the contents of a prospectus mentioned above do not apply (i) to the issue of a prospectus or form of application, to the existing members or debenture-holders of the Co. (whether a right of renunciation in favour of another person is reserved to them thereunder or not) and (ii) to the issue of a prospectus or form of application relating to issue of shares or debentures which are to be *pari passu*, i.e. in all respects uniform with shares or debentures already issued and which are being dealt in or quoted on a Recognised Stock Exchange (i.e. notified by Central Government as such in Official Gazette). Save as aforesaid, the said provisions apply to all prospectuses and forms of application, whether issued on or with reference to the formation of a Co. or subsequently thereto. The sec. does not limit the liability which any person may incur under the general law or apart from the sec. Further, the "expert" whose statement is sought to be included in a prospectus shall not be a person who is or has been engaged or interested in the promotion, formation or management of the Co. (s. 57). "Expert" includes an engineer, valuer, accountant and any other person whose profession gives authority to his statement. A prospectus inviting persons to subscribe for shares or debentures of a Co. and containing a statement by an "expert" shall not be issued unless (i) he has given his written consent to the issue thereof with the statement included and (ii) has not withdrawn his consent before it is issued (s. 58). Issuing a prospectus in contravention of ss. 57 and 58 is punishable with fine (upto Rs. 5,000) for the Co. and every person, knowingly party to the issue. Under s. 61 the terms of contract referred to in a prospectus or in a statement in lieu of prospectus, cannot at any time be varied by the Co., except subject to the approval of or except on the authority given by the Co. in general meeting.

Registering of Prospectus: (i) A copy of every prospectus signed by every person named therein as a director or proposed director of the Co. or by his agent authorised in writing shall be filed for registration with the Registrar on or before its publication

and no prospectus shall be issued until then. (ii) Further, the copy to be filed with the Registrar shall have endorsed thereon or attached thereto (a) the consent of the expert (if any) as required by s. 58 and (b) in case of a prospectus issued generally or to the public at large (i) a copy of every contract required to be specified in the prospectus by Schedule II and where the contract is oral, a Memorandum giving full particulars thereof; (ii) where adjustments as mentioned in cl. 32 have been made or indicated (without giving reasons) by persons required to make a report under Part II of Schedule II, a written statement signed by those persons and giving reasons therefor should also be endorsed on such copy or attached to the same. The Registrar shall not register a prospectus unless it is dated and a copy thereof is signed, as required by the sec. and unless further, it has endorsed thereon or attached thereto the documents (if any) mentioned above. Where a person is named therein as auditor, legal adviser, attorney, solicitor, banker or broker of the Co., it must be accompanied by a consent in writing of such persons to act as such. (iii) If a prospectus is issued without a copy thereof being delivered to the Registrar as above or if the copy delivered does not contain the endorsements and statements mentioned above, the Co. and every person knowingly party to the issue of the prospectus is liable to fine (extending to Rs. 5,000). (iv) No prospectus shall be issued more than 90 days after the date on which a copy thereof is delivered to the Registrar as aforesaid. If it is so issued, it will be deemed to be prospectus, a copy of which has not been delivered to the Registrar and therefore be punishable as such (s. 60).

Penalty for non-compliance with s. 56: According to sub-sec. (4) of s. 56, a director or other person responsible for a prospectus shall not incur any liability for non-compliance or contravention of the provisions of the sec. as regards contents of a prospectus if as regards matters not disclosed, (i) he proves that he had no knowledge thereof or (ii) if he shows that the non-compliance or contravention arose from an honest mistake of fact or (iii) if the non-compliance or contravention was as regards immaterial matter or was one which, in the opinion of the Court, ought to be reasonably excused. As regards non-disclosure of the interest of a director or promoter in the promotion of the Co. or in any property acquired by the Co. such person shall not incur liability unless it is proved that he had knowledge of the matter.

Untrue Statement in Prospectus : what is

There are two types of "untrue statements" which may be included in a prospectus and which are sought to be defined by sec. 56, viz.: (i) if the statement so included is misleading in the form and the context in which it is included: (ii) Further, an omission from the prospectus of any matter (whether required to be stated in the prospectus under s. 56 or not), which is calculated to mislead, shall also amount to an "untrue statement included in a prospectus". "Included in a prospectus" covers also a statement contained in a report or memorandum incorporated by reference with or issued with a prospectus.

Liability of Directors in case of "untrue statements" in prospectus

Directors and others who are concerned with the issue of a prospectus may incur liability in respect of "untrue statements" contained therein, in a variety of ways: (i) they may become liable in damages in respect thereof in an action for "deceit". This is an action in tort under the general law. (ii) They may incur a special liability to pay compensation to persons who subscribe for shares on the faith of such "untrue statements" under s. 62 of the Act. (iii) They may also be criminally liable for the same under s. 63 of the Act.

Liability in action for "deceit": In an action for damages for deceit, it would be necessary for the plaintiff to prove actual fraud on the part of the director concerned. As was held in *Derry v. Peek* (x), a director will not be liable in damages for a false statement in a prospectus, if he honestly believed it to be true, though there was no reasonable ground for the belief. It was with a view to remedy this defect that a special liability was created in England by the Directors' Liability Act of 1890 (counterpart of

(x) (1889), 14 A.C. 337.

which is s. 62 of the present Act): Mere silence is not deceit. Similarly an innocent misrepresentation is not deceit. The misrepresentation must be made with knowledge that it is false or in reckless disregard as to whether it is true or false (y). Further, the misstatement must be as to a material fact. Lastly the plaintiff must have been induced to enter into the contract as a result of such misrepresentation. A material contract is one which is likely to influence the mind of an intending applicant as to whether he should apply for the shares or not (z).

Special Civil Liability under s. 62: (i) Under the sec., (i) every person who is a director of the company at the time of the issue of the prospectus, (ii) or a person who has given authority to be named and is named as a director in the prospectus, (iii) every person who has given authority to be named as having agreed to become a director immediately or in the future and who is mentioned as such in the prospectus, (iv) every promoter, and (v) every person who has authorised the issue of the prospectus shall be liable to pay compensation to any person who subscribes for shares or debentures of the company for any loss or damage sustained by him by reason of "untrue statements included in the prospectus".

As regards persons mentioned above, none of them shall be liable under the sec., if he proves: (i) that having consented to become a director he withdrew his consent before the prospectus was issued and that the same was issued without his authority or consent; (ii) that the prospectus was issued without his knowledge and consent and that on knowing the same, he gave reasonable public notice that it was issued without his authority or consent or (iii) that after the issue of the prospectus and before allotment thereunder, he on becoming aware of the untrue statement, withdrew his consent to the issue and gave reasonable public notice of the same with reasons; (iv) if he proves that as regards an untrue statement purporting to be a statement by an expert or to be contained in a copy or extract of or valuation of an expert, that it was correct and fair representation of the statement or a correct copy of or extract from such report or valuation, that he had reasonable grounds to believe and did believe upto the time of the issue of the prospectus that such person was competent to make the statement, that such person had given his necessary consent under s. 58 and that he had not withdrawn his consent before the delivery of copy of the prospectus for registration or to his knowledge, before allotment; (v) as regards untrue statement, purporting to be made by an official person or contained in a copy of or extract from a public document, that it was a fair and correct representation of or extract from the same; (vi) as regards untrue statements, other than those mentioned above, if he proves that he had reasonable grounds to believe and did believe, upto the time of allotment of shares or debentures that the same were true. The protection given above cannot be availed of by an expert who has given his consent under s. 58, for wrong statement made by him as an expert.

A director whose name is mentioned in the prospectus but who has not consented to be such or who has withdrawn his consent as above, and an expert who has under s. 58 not given his consent or withdrawn his consent as above, shall be entitled to an indemnity for all damages, costs and expenses sustained by them from the directors and other person who "authorised the issue of the prospectus" [s. 62(4)]. An expert giving his consent under s. 58 and professional advisers giving their consent as required by s. 60(3)(b), shall not, by reason only of their giving such consent, be considered as persons who have "authorised the issue of the prospectus". The onus of proving reasonable grounds to believe that the expert was competent is now shifted on the directors and others. The expert himself is now liable, unless he proves his *bona fides*.

Every person made liable under the sec. is entitled to contribution from any other person who is equally liable with himself for the untrue statement for which damages are payable by the former. "Promoter", in the sec. means a promoter who is a party to the making of the prospectus or a part thereof containing the untrue statement but does not include professional advisers. (2) As regards experts giving their consent as required by s. 58 they shall not by reason of such consent alone be liable under the

(y) *Arkwright v. Newbold* (1881), 17 Ch. D. 301.

(z) *Sullivan v. Metcalf*, 5 C.P.D. 455.

sec. except for untrue statements made by them as such experts. Even as regards such untrue statements made by them, such persons shall not be liable under the sec. if they prove that: (i) having given their consent as experts under s. 58, they withdrew it in writing before a copy of the prospectus was delivered to the Registrar or (ii) that after a copy of the prospectus was delivered to the Registrar but before allotment thereunder, on their becoming aware of the untrue statement, they withdrew their consent in writing and gave reasonable public notice of their withdrawal, with reasons therefor or (iii) that they were competent to make the statement and had reasonable grounds to believe and did believe till the time of allotment, that the statement was true [s. 62(3)].

S. 62 introduces into India the remedy provided in England against directors by the Directors' Liability Act of 1890. Before that Act, directors and others, responsible for prospectus containing false and misleading statements, were liable only on an action for deceit, which action required the plaintiff to prove actual fraud in order to succeed. It was held therefore in *Derry v. Peek* (a), that if the statement was made under an honest belief that it was true, the directors would not be liable. It was in order to get rid of the effect of this decision that the Directors' Liability Act of 1890 was passed and the same law is introduced into India by this sec. By the sec. the onus of proof is shifted on the director to prove that he is innocent. As soon as the plaintiff proves (i) that the defendant was responsible for the mis-statement in the prospectus, (ii) that he bought shares on the footing that the statement was true, and (iii) that he has been damnified, the defendant director or other relevant person would be liable, unless he proves that he comes under any of the exceptions to the sec. Under exception (vi), it is necessary that the director and other person making the statement must have reasonable grounds to believe that the statement was true. Thus it has been held in an English case that the uncorroborated statements of a vendor or promoter of a company, afford no reasonable grounds for believing them to be true and misleading statements made in a prospectus on the faith of such statements will not be protected as statements made on the report of an expert (b). But for honest errors of judgment, directors are not liable, provided they acted with reasonable care. Where a Co. was formed to take over and work a rubber plantation from a syndicate and the directors issued a prospectus containing untrue statements as regards the area and the number of trees on the estate, but the statements were made on information from a member of a firm from which the syndicate had purchased the estate, it was held that the directors were not guilty of gross negligence in believing the information and were, therefore, not liable as on a misfeasance (c).

Criminal Liability: Under sec. 63, a person who, after the commencement of the Act, authorises the issue of a prospectus, containing an "untrue statement" is punishable with imprisonment upto 2 years or a fine upto Rs. 5,000 or both, unless he proves either that the statement is immaterial or that he had reasonable grounds to believe, and did believe, the same to be true upto the time of the issue of the prospectus. An expert consenting to his statement being mentioned in the prospectus under s. 58 and professional advisers mentioned in s. 60(b) (3) who consent to their names being mentioned as such in the prospectus, are not to be deemed to have "authorised the issue of the prospectus" by reason of such consent only.

A person wilfully issuing a false prospectus, whether he is a director, promoter or any other person, is also liable to be prosecuted under s. 628 of the Act. The case of *Rex v. Kysant* (d), is a recent illustration of this: In that case, Lord Kysant, who was the managing director of the Royal Mail Steam Packet Company, issued a prospectus for issue of fresh debenture stock. Every statement in the prospectus, taken by itself, was true, but it omitted to state several facts, which if stated would have removed the illusion of soundness and stability of the concern, which was sought to be created by the document. In particular, while mentioning that dividends were regularly paid by the company, during some of the lean years, it failed to state that those dividends were not paid out of profits (for in fact, there were large losses during those years), but out of items of non-recurring nature, i.e. refund of excess profits duties, etc. It was held

(a) 14 A.C. 337.

(b) *Adams v. Thrifts* (1915), 1 Ch. 557.

(c) *Re Brazilian Rubber Plantations* (1911), 1 Ch. 425.

(d) (1932), 1 K.B. 442.

on these facts by the House of Lords that Lord Kylsant was rightly convicted under the Larceny Act (similar to s. 628 of the Act).

Effect of "untrue statement" on contract to take shares, etc.: A prospectus may be false or misleading in a variety of ways. It may be misleading because of untrue statements contained therein. It may also be misleading because it does not disclose all the material facts. Different kinds of rights and liabilities arise, in each of the above two cases.

As regards "*untrue statements*": (i) when the prospectus contains misstatements of such a nature that the whole prospectus becomes a *fraudulent* document, the party who is induced by such fraud to subscribe for shares, debentures or debenture stock, is entitled to rescind the contract and to ask that his name be taken off the register of members (e).

(ii) If the misrepresentation is *innocent*, the contract to take shares can still be set aside and the applicant can claim to have his name struck off the register. Thus where a company was formed to work certain silver mines and the prospectus, on the faith of which the plaintiff had bought shares, contained statements that valuable silver mines had been found and it turned out that the mines were valueless and the directors at the time of issue of the prospectus were not aware of the truth or otherwise of the statements made by them regarding the said mines, *held*, the shareholder was entitled to repudiate the shares. Per Lord Cairns, "if persons make assertions of facts as to which they are ignorant whether the assertions are true or untrue, they become in a civil point of view as responsible as if they had asserted that which they knew to be untrue" (f). If an application for shares is made on the faith of a statement in a prospectus which is true when made but which is not true when the shares are allotted to the applicant, the latter is entitled to rescind the contract (g).

Under s. 71 the contract is not *ab initio* void but voidable at the instance of the allottee. If he wishes to avoid he must take legal steps to have it avoided. The limit of time prescribed is 2 months after the statutory meeting, notwithstanding the fact the liquidation has supervened.

Non-disclosure does not entitle a shareholder to rescind the contract (h). He can only recover damages (if any) caused to him by the default (i), provided the non-disclosure was of a material fact (j). A non-disclosure of their interest by the directors, may make them liable to account to the company for the secret profits they may have made.

A concealment may be of such a nature that, together with what is disclosed, the whole prospectus may become a fraudulent document. As Lord Macnaughton said in *Gluckstein v. Barnes* (k), "sometimes half a truth is no better than downright falsehood". In such a case, it is presumed that a shareholder will have a right to rescind the contract.

Statement in Lieu of Prospectus: According to sec. 70 where a Co., having a share capital, does not issue a prospectus on or with reference to its formation, or having issued a prospectus, has not proceeded to allot shares offered to the public for subscription, the Co. shall not allot any shares or debentures unless, at least three days before the first allotment, it has delivered to the Registrar for registration a "statement in lieu of prospectus": Such a "statement" must be signed by every director or proposed director mentioned therein or by their agents authorised in writing. It must contain particulars mentioned in Part I of Schedule III and set out reports mentioned in Part II of Schedule III subject to the provisions of Part III of Schedule III. Where persons making Reports have made or indicated adjustments as mentioned in cl. 5 of Schedule III, the "statement" must have endorsed thereon or attached thereto, written statement

(e) *Houldsworth v. Glasgow Bank* (1880) A.C. 317.

(f) *Rees River Silver Mining Co. v. Smith*, 4 H.L. 64.

(g) *Re Kent County Gas Co.* (1917) L.T. 756.

(h) *Re Wimbledon Olympia* (1910), 1 Ch. 630.

(i) *Re South of England Gas Co.* (1911) 1 Ch. 537.

(j) *Nash v. Galthorpe* (1905), 2 Ch. 237

(k) *Supra*.

signed by such persons, setting out the adjustments and the reasons therefor. The Co. and every director who wilfully authorises or permits a contravention of the above is liable to a fine extending to Rs. 1,000. The provisions of the sec. do not apply to private company.

Contents of "statement" in lieu of prospectus [s. 70, cl. (2)]: The "statement" is, in effect, a prospectus in an abbreviated form. It must contain the following items out of those mentioned at page 305 before, viz. (i), (ii), (iii), (vi), (ix), (xii), (xiii), (xvi), (xvii), (xix), (xx), (xxi), (xxii), (xxiii) and (xxiv). Out of reports the following, viz. items (ii) and (iii) p. 307 (*ante*) must be set out.

"Untrue Statement" [s. 70, cl. (6)]: A statement included in a "statement in lieu of prospectus" is deemed to be "untrue" if it is misleading in the form and context in which it is included. The omission of a statement required to be mentioned under s. 69, cl. 2, shall be deemed to be "untrue", if "calculated to mislead". "Included" here means included in the "statement" or in any report or memorandum attached thereto or endorsed thereon or by reference incorporated therewith.

Consequences of "Untrue Statement" [s. 70, cl. (5)]: Where the "statement" delivered to the Registrar includes an "untrue statement", any person authorising the delivery of the statement for registration shall be liable to imprisonment extending to two years or fine extending to Rs. 5,000 or both, unless he proves (i) that the "untrue statement" was immaterial or (ii) that he had reasonable cause to believe and did believe that the statement was true upto the time the statement was delivered for registration. An allotment of shares is not bad because the statement filed under the sec. is untrue or misleading, but if shares have been bought on the faith of such statement, the contract can be rescinded (l). If allotment is made, without filing the "statement in lieu of prospectus", the allotment is not absolutely void but voidable at the instance of the Co (m). A person wilfully making a false statement in the above document is liable to prosecution under s. 628. Notice that the provisions of s. 62 do not apply to this document.

To check the activities of what Lord Atkins calls "share pushers", which involve grave danger to the community, the Act has put certain statutory restrictions on "offers" of shares and debentures to the public. Under sec. 56(3), it is illegal to issue any form of application for shares or debentures of a Co., unless the form is accompanied by a prospectus which complies with the requirements of s. 56 above. The provision however is not to apply where a *bona fide* invitation has been issued to a person to enter into an underwriting agreement with regard to the shares or debentures or where the shares or debentures are not offered to the public. Any person acting in contravention of the above is punishable with a fine extending to Rs. 5,000. Notice, however, that a contravention of the sec. does not make the contract to take shares void. The only consequence of non-compliance with the sec. is a penalty for the offending parties (n).

A new form of liability is created by sec. 68 with regard to persons who fraudulently either alone or with others, induce the public to invest their moneys in bogus concerns. The sec. is based on s. 12 of British Prevention of Frauds (Investment) Act, 1939. Under the sec. a person who by knowingly or recklessly making any false, deceptive or misleading statement, promise or forecast or by dishonest concealment of material facts, induces (or attempts to induce) another to enter (or offer to enter) into: (i) an agreement for the acquisition, disposal, subscribing or underwriting of shares or debentures or (ii) an agreement for securing profit to any party thereto from the yield of or from the fluctuations in the value of the shares or debentures is punishable with imprisonment upto 5 years or fine upto Rs. 10,000 or both. A conspiracy to commit the above offences is also similarly punishable.

Offering shares for sale: Where shares or debentures are allotted or agreed to be allotted by a Co. for the purpose of the shares or debentures being subsequently offered to the public for sale, the offer shall be deemed to be a "prospectus" and it shall conform

(l) *Re Blair Open Hearth Furnace Co. Ltd.* (1914), 1 Ch. 390.

(m) *Re Jubilee Cotton Mills* (1924) A.C.

925.

(n) *Mansukhlal v. Jupiter Airways*, 54 Bom. L.R. 777.

to all the requirements mentioned in s. 56, as to prospectus; further, the following particulars shall be added: (i) net consideration received or to be received by the Co. in respect of shares or debentures offered and (ii) place and time at which the contract under which allotment is made can be inspected. Persons making the offer shall, for purposes of s. 60, be deemed to be persons named as directors in the prospectus. If the offer to the public is made by a firm or a Co., the document containing the offer shall be signed by two directors or one-half of the partners of the firm as the case may be (if necessary by agent authorised in writing). All provisions as regards liability in respect of prospectus shall apply to the document in question. For the above purposes, an allotment or an agreement to allot shares and debentures shall be deemed to be made with a view to offering the same to the public for sale if (i) an offer of the said shares and debentures or any part of them is made to the public within 6 months of the allotment or agreement to allot or (ii) if at the date of the offer to the public, the whole consideration for the said shares and debentures has not been received by the Co. (s. 64).

Promoters, who are: S. 62 in terms refers to promoters. The word "promoter" has no definite meaning. It is not a term of law but of business having a meaning in the commercial world. It is not everybody who is connected with the formation of a company who can be called a promoter. Thus, professional advisers, legal as well as others, are not promoters. Similarly where those engaged in starting a new enterprise, engage the services of experts to put them in possession of the full facts with regard to the proposed enterprise and its future prospects, e.g. valuers, surveyors, engineers, etc., they cannot be called "promoters". The word was defined by Cockburn C.J. as "one who undertakes to form a company with reference to a given project and to set it going and to take the necessary steps to achieve the purpose" (o). As Lord Blackburn stated in *Erlanger v. New Sombrero Phosphate Co.* (p), "it is a short and convenient way of designating those who set in motion the machinery by which the Act enables them to create an incorporated company".

Duties of Promoters: The legal position of a promoter is somewhat peculiar. He is not a trustee for the Co. because there is no Co. yet in existence. For the same reason he cannot be the agent of the Co. also. The correct way to describe his position in law is that he stands in fiduciary position towards the Co. about to be formed, in the same way as a director does. Two important results follow from this: (i) a promoter cannot be allowed to make any secret profits. If it is found that in any particular transaction for the Co., the promoter has obtained a secret profit for himself, he will be bound to refund the same to the Co. (q). (ii) He is not allowed to derive a profit from the sale of his own property, unless all material facts are disclosed. If a promoter contracts to sell to the Co. a property without making a full disclosure, and the property was acquired by him at a time when he stood in a fiduciary position to the Co., the Co. may either rescind the sale or affirm the contract and recover the profit made out of it by the promoter (r). The disclosure may be made (a) to an independent board of directors, or (b) in the articles of association, or (c) in the prospectus, or (d) to intending shareholders direct.

Liability of Promoters: He is liable to account to the Co. for all secret profits made by him without full disclosure to the Co. The Co. can also sue for rescission of a contract of sale by the promoter to the Co. which is vitiated by non-disclosure of his own interest therein (s). The Co. can also proceed against a promoter on action for deceit or breach of duty by way of misfeasance summons (under s. 543) if loss is caused by the Co. by such breach (t).

Promoters and the "Preliminary Contract": This is a peculiar kind of contract which is often entered into by Co.s or on behalf of Co.s. Where Co.s are formed for the purpose of purchasing an existing business or property or where it is necessary for a Co. about to be formed, to acquire some property or right, in order to carry on

(o) *Twycross v. Grant*, 2 C.P.D. 469, 471.

(p) (1878), 3 A.C. 1268.

(q) *Sydney Iron Ore Co. v. Bird* (1886), 3 C.D. 91.

(r) *Erlanger v. New Sombrero Phosphate Co.*, 3 A.C. 1218.

(s) *Ibid.*

(t) *Cavendish Bentick v. Fenn* (1887), 12 A.C. 652.

its business, the promoters of the Co., before the Co. is formed, enter into a contract with the owner of that property or right, to acquire the same for and on behalf of the Co. Such contracts are called "preliminary contracts". Their position at law is somewhat peculiar. The promoter enters into the preliminary contract with the vendor, generally as agent or trustee for the Co. about to be formed. But a person cannot act as the agent or trustee of another who is not yet in existence. The result of this position is threefold: (i) the Co. when it comes into being is not bound by the contract; (ii) the Co. cannot sue the vendor on the contract. Lastly, (iii) the agent himself remains personally liable on the contract, even if it is afterwards ratified by the Co. (u). These contracts, therefore, generally also provide: (i) that if the Co. adopts the agreement, the agent's liability shall cease and (ii) if the Co. does not adopt the agreement within a certain time, either party may rescind the contract. In such a case, the agent's responsibility in any case would cease after the lapse of the fixed time. If the Co. adopts the agreement, it will enter into a new contract with the vendor directly after incorporation.

ALLOTMENT OF SHARES

Allotment Generally: Allotment is the appropriation of a certain number of shares to a specified person who has applied for them. It is usually done by a resolution of the board of directors. Allotment is governed by the general principles of the law of contract. An application for shares is an offer, the allotment is an acceptance of that offer. The acceptance is not complete till the fact of allotment is communicated to the applicant. Thus a mere application for shares and an allotment of the shares by the Co. to the shareholder will not make the latter liable as a member of the Co. (v). There may, however, be a valid executory contract for allotment of shares by an offer and a communicated acceptance, even before an allotment in fact has been made (w). Ordinarily, the acceptance by the Co. is not complete till the letter of acceptance is posted. If the letter of acceptance is lost, the allottee will be liable (x). Similarly, if it is delayed, the allottee's repudiation in the meanwhile will not avail (y). If there is undue delay in allotment, the offer to take shares will lapse. Thus where M applied for shares in June and shares were not allotted till November, *held*, the offer had lapsed before its acceptance (z). This case was followed by the Bombay High Court (a), where a person had applied for 600 shares of a Co, and paid the application moneys in respect thereof on 23rd August 1919. On 3rd August 1920 the Co. allotted the said shares to him but no notice of allotment was given. The Co. also failed to give notice as to payment of the remaining amount on the shares, which was by the articles payable within 60 days of the allotment. The time for payment was extended upto May 1921 but no payment was made. On 17th March 1925 the Co. passed a resolution under another article forfeiting the shares and in January 1928 filed a suit to recover the balance of the amount due in respect of the shares. *Held*, the allotment not being within a reasonable time, the defendant was entitled to repudiate the same, and that he could do so for the first time in the suit, because the fact of allotment was never communicated to him. Further, that as no time for payment of money was ever fixed, the article as to forfeiture did not apply.

Conditions for Allotment of Shares: In case of Co.s offering shares for public subscription, no allotment of shares shall be made, unless (i) the amount stated in the prospectus as the minimum amount which in the opinion of the directors must be raised by the issue of share capital in order to provide for "*the minimum subscription*" has been subscribed and (ii) the sum payable on application [which shall not be less than 5% of the nominal amount of the shares] has been paid to and received by the Co. in cash or by cheque (which has been honoured). Notice that the amount of "*minimum subscription*" as stated in the prospectus, has to be calculated for the above

(u) *Kilner v. Baxter* (1866) L.R. 2 C.P.

174. (v) *Gunn's Case* (1867) L.R. 3 Ch.App.

40. (w) *Bai Mangu v. Bharatkhand Cotton Mills*, 32 Bom. L.R. 812.

(x) *Harris' Case* (1872), 7 Ch.App. 587.

(y) *Dunlop v. Higgins* (1848), 1 H.L.C. 381.

(z) *Ramsgate Hotel Co. v. Montifiori* (1886) L.R. 1 Ex. 109.

(a) *Indian Co-operative St. N. Co. v. Padamsi*, 36 Bom. L.R. 32.

purpose, exclusive of any amount payable otherwise than in cash. (For "minimum subscription" see p. 306, cl. ix.) The amount received from applicants as above must be deposited and kept deposited in a Scheduled Bank until returned to the applicants as hereinafter provided or until the "certificate to commence business" is obtained. Every promoter, director or other person, who knowingly contravenes the last provision shall be punishable with fine (upto Rs. 5,000). If the "minimum subscription" is not subscribed for or if the amount payable in respect thereof is not paid within 120 days after the first issue of the prospectus, all money received from the applicants for shares shall be forthwith paid to them without interest. If any such money is not so repaid within 130 days after the issue of the prospectus, the directors shall be jointly and severally liable to repay the said moneys with interest at 6 per cent per annum from the 130th day, provided that a director shall not be liable if he proves that the default in repayment was not due to any misconduct or negligence on his part. A condition requiring an applicant for shares to waive a breach of the above requirements is void. The sec., except the provision as to the amount payable on application, shall not apply to any allotment of shares subsequent to the first allotment offered to the public for subscription (s. 69).

Where a Co., having share capital, does not issue a prospectus with reference to the formation, or where having issued a prospectus, it has not proceeded to allot shares offered to the public, it shall not allot any shares or debentures unless, at least 3 days before the first allotment of the same, a "*statement in lieu of prospectus*" containing the required particulars (see *ante*), signed by every person named therein as director or proposed director (or by his agent), has been delivered to the Registrar for registration. Where in any such "*statement in lieu of prospectus*" adjustments have been made in any reports attached thereto (as mentioned in cl. 5 of Schedule II), it shall have endorsed thereon a statement signed by those persons, setting out the adjustments and the reasons therefor. A Co. and any director thereof acting in contravention of the above is liable to a fine extending to Rs. 1,000 (s. 70). Notice that the sec. does not apply to a private Co. (b).

Avoiding Irregular Allotment: Where a Co. makes an allotment in contravention of the provisions of ss. 69-70 it shall be voidable at the instance of the applicant within 2 months of the holding of the statutory meeting and not later, and where a Co. is not required to hold statutory meeting or where the allotment is made after the statutory meeting, within 2 months after the allotment and not later; and shall be so voidable, notwithstanding that the Co. is in course of being wound up. A director knowingly contravening or wilfully authorising or permitting contravention of the provisions of ss. 69-70 with respect to allotment shall be liable to compensate the Co. and the allottees for all loss, damages and costs caused to them thereby, provided proceedings therefor are started within 2 years of the allotment (s. 71). Notice that a shareholder, who after notice of the irregularity, acquiesces in the allotment, will not be entitled to repudiate the same (c).

Under s. 72, no allotment of shares or debentures shall be made before the beginning of the 5th day after general issue of the prospectus or any other longer date mentioned in the prospectus, nor shall any proceedings be taken on applications made in pursuance of such a prospectus, till such date. If after the general issue of a prospectus, a public notice is given by any person mentioned in s. 62, whereby his liability is excluded, limited or diminished, the above five days shall be counted from after publication of such notice. Such date is called "*the time of opening of subscription lists*". Where the prospectus is issued generally by way of newspaper advertisement, the five days shall be counted as from date of such publication. A contravention of the above does not invalidate the allotment but the Co. and every officer in default is liable to a fine (upto Rs. 5,000). Where shares or debentures are offered for sale, the above rules are similarly applicable, the person liable for contravention in such a case being the person by or through whom the offer is made. An application for shares in pursuance of a prospectus issued generally, cannot be revoked till after the expiry of the fifth day of the opening

(b) Laxmi Narshi Reddi v. Off. Receiver
(1951), 1 Mad. L.J. 488.

(c) Finance & Issue Ltd. v. Canadian
Produce (1905), 1 Ch. 37.

of the subscription list or the publication of a notice by any person mentioned in s. 62 excluding his liability as aforesaid.

Allotment of shares to be quoted on Stock Exchange: Where a prospectus issued generally or otherwise states that permission for dealing with the shares or debentures offered thereby on a "recognised stock exchange" has been or will be asked for, any allotment thereof shall be void, if no permission has been applied for within 10 days of the issue of the prospectus, or if permission is not granted before expiry of three weeks, from the date of closing of the subscription lists (or 6 weeks, if notice in that behalf has been given to the applicant within the 3 weeks). If permission is not so applied for or not granted as aforesaid, the directors shall repay forthwith all moneys received in pursuance of such prospectus to the applicants and if the moneys are not so paid within 8 days after they have become so payable, the Co. and the directors shall be jointly and severally liable to repay the same with interest at 5% from the 8th day. A director, however, shall not be liable if the default has not been due to any negligence on his part. All moneys received in such cases shall be kept in separate account in a Scheduled Bank till the Co. is liable to repay the same as above. Contravention of above makes the Co. and every officer in default liable to a fine (upto Rs. 5,000). Any condition in a prospectus binding the applicant to waive the above provisions will be void (s. 73). The Stock Exchange mentioned above must be a "recognized Stock Exchange". Permission will not be deemed to be refused if the matter is stated to be under consideration. Prospectus generally mentions when the subscription list will be closed. The above provisions also apply in favour of an underwriter of shares or debentures, who has underwritten the issues. They also apply where shares are offered for sale. In such cases, the person by or through whom the offer is made shall be liable to repay as above and the person liable for contravention shall also be the same person under the same conditions. In counting the above period of five, eight and ten days, public holidays under the Nego. Insts. Act shall be disregarded. If the period expires on a holiday, the next day thereafter shall be substituted therefor (s. 74). Opinion has been expressed in England that the above provisions for refund would create a trust in favour of the applicants (d).

Return as to Allotment: Where a Co. having a share capital makes any allotment of shares, it shall, within one month thereafter (i) file with the Registrar a return of the allotment showing the number and nominal amount of shares comprised in the allotment, the names, addresses and occupation of the allottees and the amount (if any) paid or due and payable on each share; (ii) in cases of shares allotted as fully or partly "paid otherwise than in cash" produce before the Registrar for his inspection and examination, a contract in writing constituting the title of the allottee to the allotment together with any contract of sale or for services or other consideration for the allotment (duly stamped). Copies of such contracts, etc. verified in the prescribed manner shall also be filed with the Registrar, together with a return, stating the number of shares so allotted, the extent to which they are to be treated as paid up and the consideration for which they are so allotted. In case of bonus shares the Co. must file with the Registrar within the above period, a return showing the number and nominal amounts of shares as allotted. (iii) If such a contract is not reduced to writing, the Co., within one month of the allotment, must file with the Registrar, particulars in writing of such contract and those particulars should be stamped with the same duty as would be payable on that contract, if it had originally been reduced to writing. The Registrar has power to extend the period of one month if he is satisfied that the period is inadequate. (iv) In case of default, every officer of the Co. who is in default, is liable to a fine (upto Rs. 500 per day the default continues). (v) The Court, however, in case of failure to file with the Registrar within the time specified, any document required to be filed under the sec., may, on the application of the Co. or any officer in default, if satisfied that the omission was due to accident or inadvertence or that it is otherwise just and equitable to grant relief, extend the time within which to file such document for such period as it may think proper. Nothing in the sec. applies to the issue and allotment of shares, which have been forfeited by the Co. for non-payment of calls (s. 75). For "payment otherwise than in cash" see seq.

COMMISSION AND DISCOUNT

Payment for Shares : It is a fundamental principle of Company Law that a person who buys shares must pay to the Co. the whole nominal amount of his shares in cash. Thus if a person wants to buy £1 share, he has got to pay £1 to the Co. for the share. If he pays less, or if the Co. agrees to take anything less from him, he would be liable on winding up for the amount unpaid on his shares. "Cash", however, does not mean actual coin, but anything of value, i.e. "such a transaction as would, in an action at law for calls, support a plea of payment".

Where shares are issued in consideration of any other thing than a money payment, they are said to be issued, for "*consideration other than cash*". This is permissible under the Act, provided certain conditions are fulfilled. These are laid down by s. 75, which provides that where shares are allotted as fully or partly paid up otherwise than in cash, the Co. must, within one month of the allotment, produce before the Registrar, a contract in writing, constituting the title of the allottee to the allotment of those shares, and also any contract of sale or for service or other consideration, in respect of which shares are allotted, together with a statement or return, showing the number and the nominal amount of shares so allotted, the extent to which they are treated as paid up and the consideration for which they have been allotted. If the original contract is not in writing, prescribed particulars of the contract must be filed with the Registrar, within the same time (see *ante*).

Issuing Shares at Discount Prohibited : It is a fundamental rule of Company Law that the registered capital of a Co. is to be always regarded as sacrosanct and that a Co. cannot allow any discount on shares, that is to say, it cannot issue shares for a consideration less than the nominal amount of the shares. This is clearly stated in cl. (ii) (s. 76) which provides that save as laid down in that sec. and s. 79 (see below), no Co. shall allot its shares or apply its capital money or debentures either directly or indirectly in payment of any commission, discount or allowance to any person in consideration of his subscribing or agreeing to subscribe, or procuring or agreeing to procure subscriptions for its shares or debentures. The agreement may be conditional or absolute and so also the subscription. Such payment of commission or discount, by way of payment of money, or shares or debenture in the Co., cannot be made by adding to the purchase price of the property acquired, or to the contract price of work to be executed for the Co. It cannot be paid out of the nominal purchase price or contract price or otherwise howsoever also (*Ibid*). The rule applies to public as well as private Co.s. The reason of this is that to allow otherwise, would amount to a reduction of capital which the law does not permit, except under stringent conditions. To this principle, however, there are certain exceptions: Thus, (i) a Co. may pay "commission", otherwise known "*underwriting commission*", in respect of its shares or debentures. This is allowed by s. 76. (ii) It can also give "*brokerage*" for "*placing*" its shares. (iii) A limited power has been given to Co.s by s. 79 to issue shares at a discount under certain conditions. (iv) A Co. is now allowed to issue redeemable preference shares under s. 80. (v) Forfeited shares can be issued at a discount. Excepting these statutory cases, the rule, however, still remains, that a Co. cannot reduce its capital by indirect methods and particularly that it cannot issue shares at a discount.

Underwriting Commission : Sec. 76 provides that it shall be lawful for a Co. to pay commission to any person in consideration of his subscribing or agreeing to subscribe, absolutely or conditionally or procuring or agreeing to procure subscriptions, absolute or conditional, for shares or debentures of the Co. if: (i) the payment of commission is authorised by the articles, (ii) the commission paid or agreed to be paid does not exceed 5 per cent of the issue price of the shares or the amount or rate specified in the prospectus (whichever is less) and in case of debentures, two and a half per cent of the issue price or the rate authorised by the articles (whichever is less), (iii) and the rate or the amount is disclosed in the prospectus in case of Co.'s offering shares or debentures to the public and in case of Co.s not so offering, is disclosed in "the statement in lieu of prospectus", or in a statement in the prescribed form signed in the like manner as "statement in lieu of prospectus" and filed with the Registrar and where a circular or notice is issued, disclosed in the same, (iv) the number of shares or debentures which

persons have agreed for a commission to subscribe (absolutely or conditionally) is also disclosed as aforesaid.

S. 76 further provides that (i) the power of a Co. to pay brokerage which has been lawful for it to pay heretofore is not affected and (ii) a vendor or promoter or other person who receives payment in money, shares or debentures, from the Co. shall always be deemed to have the power to apply any part thereof to the payment of any commission, which it would have been lawful for the Co. to pay directly under the sec. (iii) On contravention of above provisions, the Co. and every officer in default is punishable with a fine (upto Rs. 500). Under the sec., where a Co. has paid commission in respect of any shares or debentures or allowed any sums by way of discount, in respect of any debentures, it shall state in each balance sheet the total amount so paid or allowed or so much thereof as has not been written off till the whole amount is written off. (iv) Notice that under the sec., the prohibition is against the use of "shares, debentures or capital moneys". Commission can be paid out of "share premium account" or from "redemption reserve fund". Art. 5 of Table A provides that rate of commission shall not be more than 5% of the price at which the shares are issued. The commission can be paid in cash or in partly paid-up shares or partly in one and partly in the other. An "underwriting agreement" is an agreement whereby previously to the offer of the shares of a Co. to the public for subscription, some person undertakes in consideration of a commission, to take the whole or a portion of such (if any) shares as may not be subscribed for by the public (Rawlins and Macnaughton). "Placing" means procuring others to take the shares. Underwriters, sometimes, enter into subsidiary contracts with other parties to protect themselves from possible loss. This is called "sub-underwriting". Commission paid to sub-underwriters must now be disclosed in the prospectus [see Sch. II, Part I(13)]. "Brokerage" is different. It refers to commission paid to professional brokers, stock-brokers, bankers and the like who exhibit the prospectus of the Co. in their place of business and send copies to their customers and by whose mediation customers are induced to buy shares (e).

Purchase of or Loans for Purchasing its Own Shares by Company Prohibited: S. 77 provides that no Co. limited by shares and no guarantee Co. having a share capital can buy its own shares except as (i) provided by above sec. or (ii) by ss. 100-104 or (iii) by s. 402 (by way of preventing oppression). Further, no public Co. and no private Co. (being subsidiary of a public Co.) can give financial aid to any person (either directly or indirectly, by way of loan, guarantee or security) for purchase or subscription of any shares of its own or of its holding Co. On contravention of the above, the Co. and every officer in default is liable to a fine.

Exceptions: The sec. does not prohibit: (i) loans by banking Co.s in course of their business, (ii) provision by a Co., in accordance with any scheme, of money for purchase or subscription of fully paid shares of the Co. or its holding Co. to trustees for benefit of employees of the Co. (including in the term, a salaried director of the Co.). Such loans, however, shall not exceed 6 months' salary or wages of that person and (iii) the right of the Co. to redeem its shares under s. 80 or corresponding provisions of earlier Companies Acts.

The sec. is an extension of the principle established since *Trevor v. Whitworth* (f), that a Co. cannot purchase its own shares. Under the sec. both subscription and purchase are prohibited. Financial aid given in contravention of the sec. does not make the contract of purchase invalid (g) nor does the security similarly given become invalid (h). Financial aid given for purchase of shares of a subsidiary is not prohibited. Outstanding loans under cls. (b) and (c) of the sec. must be shown in the balance sheet. The person who sells shares to the Co. remains liable as a shareholder and his name can be restored on the Register (i).

Issue of Shares at Premium: Where shares are issued by a Co. at premium (in cash or otherwise), a sum equal to the aggregate amount of the premium or value shall be

(e) *Andrews Zinc Mines Ltd.* (1928), 2 K.B. 455.

(f) (1887), 12 A.C. 409.

(g) *Spink v. Spink* (1936) Ch. 544.

(h) *Victor Battery Co. v. Curry's Ltd.* (1946) Ch. 242.

(i) *General Property Investment Co. v. Matheson's Trust* (1888), 16 R.R. 282.

transferred to an account called the "*share premium account*". Amounts to the credit of this account shall be regarded as paid-up capital of the Co., for purpose of reduction of capital except as follows: the Co. can use the amount: (i) for paying up unissued shares of the Co. and issuing them to members as fully paid shares, (ii) for writing off preliminary expenses of the Co., (iii) for writing off expenses re. issue of shares, or debentures, or commission or discount paid with respect thereto, (iv) for paying premium payable with regard to redeemable preference shares or debentures of the Co. Where shares have been issued by a Co. at premium before commencement of the present Act, such part of the premium as does not form an identifiable part of the Co.'s reserves at the time, shall be disregarded for the purposes of the above account (s. 78).

Issuing Shares at Discount, when allowed: A limited power is given by the Act, to Co.s to issue shares at a discount. Under s. 79, except as provided by the sec., it shall not be lawful for a Co. to issue shares at a discount, of the class already issued, unless: (i) the issue is authorised by a resolution passed at a general meeting, (ii) the issue is sanctioned by the Court; (iii) the resolution specifies the maximum rate of discount (not exceeding 10% or such higher percentage as the Central Government may permit in special cases), at which they are to be issued, (iv) not less than 1 year has elapsed at the date of issue, since the Co. was "entitled to commence business" (see seq.); (iv) the shares are issued within 2 months of the Court's sanction or such further time as the Court may allow. Where a resolution is passed by a Co. as above to issue shares at a discount, it may apply to the Court for sanction and if the Court after having regard to all the circumstances, thinks it proper, it may sanction the issue on such terms and conditions as it thinks just. Where shares are issued at a discount, every prospectus relating to such shares, shall state the discount allowed or so much thereof as has not been written off at the date of the issue of the prospectus. Penalty for failure, to do thus, for the Co. and officer in default is a fine (upto Rs. 50).

If a shareholder has paid less than the nominal amount of the share, as consideration for the share, the shareholder will be bound to pay the balance to the Co. in spite of any agreement or contract between the Co. and the shareholder to the contrary (j). Such an agreement is not binding on the liquidator, nor, it has been held, on the Co. itself while a going concern (k).

Issue of Redeemable Preference Shares: Subject to the conditions laid down by s. 80, a Co. may issue preference shares which are redeemable by the Co. or are redeemable by the Co. at its option. The conditions are: (i) such issue must be authorised by the articles. (ii) The shares can be redeemed only out of the profits available for dividend or out of proceeds of a fresh issue made for such redemption. (iii) If premium is payable for such redemption it shall be provided out of the profits of the Co. or out of the Co.'s "share premium account", before redemption. (iv) Where such shares are redeemed out of the divisible profits of the Co., there shall be transferred, out of profits available for dividend, to a reserve fund, called "*capital redemption reserve fund*", a sum equal to the nominal amount of the shares redeemed. This fund shall be regarded as part of paid-up capital of the Co. for the purposes of reduction of capital, except as otherwise provided hereafter. (v) Subject to the above, redemption can be effected in such manner and at such time as the articles provide. (vi) Such redemption shall not be regarded as reduction of the Co.'s authorised capital. (vii) Where a Co. redeems or is about to redeem such preference shares, it shall have power to issue new shares upto the nominal amount of such preference shares; and for purposes of stamp duty (under s. 596) such new issue shall not be regarded as increase of capital, but for this purpose, new shares must have been issued within two months of the redemption. (viii) The "capital redemption reserve fund" can be applied in paying up unissued shares which are then issued as bonus shares to members. (ix) Penalty for contravention of the above provisions is a fine (upto Rs. 1,000) for Co. and every officer in default. These shares are issued by a Co. as a means of raising further capital for the purposes of its business. The sec. does not authorise conversion of shares already issued, into redeemable preference shares under a scheme or otherwise (l).

(j) Re Wragg (1897) 1 Ch. 796.

(k) Re Pilkington and Co. Ltd. (1916), 85

L.J.Ch. 318.

(l) St. James Court Ltd. (1944) Ch. 6.

Further Issue of Capital: Under s. 81 where after the first allotment of shares, a Co. desires to increase its *subscribed capital* by a further issue of shares, the following rules shall be observed, subject to any directions to the contrary given by the Co. in general meeting: (i) the new shares shall be offered to the holders of the "equity capital" of the Co. at the date of the issue, in proportion, as nearly as possible to the paid-up amount on those shares; (ii) the offer must be made by notice specifying the number of shares offered and fixing time (not being less than 15 days) within which if the offer is not accepted, it will be treated as declined; (iii) unless the articles otherwise provide, the offer shall include and specifically mention the right of the offeree to renounce the offered shares in favour of any other person; this right however is not to be allowed to extend the time fixed within which the offer is to be accepted or to permit an exercise of the right of renunciation for a second time; (iv) after expiry of time fixed or earlier (if refusal is received earlier), the directors shall dispose of the shares in the manner most beneficial to the Co. The sec. does not apply to private Co. It has been held that a receiver appointed in a dispute between the transferor and transferee of shares, has no right to apply for new shares issued by a Co. (m).

SHARE CAPITAL

Nature of Shares: A share has been defined by Farewell, J. in *Borland Trusts v. Steel Bros. and Co.* (n), as "the interest of the shareholders in the company measured by a sum of money, for the purpose of liability in the first place and of interest in the second, but also consisting of a series of mutual covenants entered into by all the shareholders *inter se*. A share is not a sum of money, but is an interest measured in a sum of money, and made up of various rights, contained in the contract". This, however, is the legal position of "shares" under English Law. Under the Indian Companies Act, "shares" are "goods" as laid down by s. 82 of the Act. The sec. provides that "shares or other interest of any member in a Company shall be moveable property, transferable in the manner provided by the articles of the Co. Each share in a Co. having a share capital shall be distinguished by its appropriate number" (s. 83).

Subject to the provisions of the Act and the Memo. (if any), a Co. may issue shares of different classes with such preferred, or other special rights or with such restrictions as to dividend, return of capital or otherwise as it may think proper. (See however s. 88 of the present Act, which prohibits such differentiation, except as regards preference shares.) Usually the power to create such classes of shares with different rights is given by the Memo. or articles. If no such power is given by either, the Co. can give itself the power by altering its articles (o). If the Memo. fixes the rights of each class, the Co. cannot alter them unless the power to do so is reserved in the Memo. (p) or the sanction of the Court is obtained under s. 17 to alter the Memo., such rights being regarded as "conditions" (q). Where, however, the Memo. gives power to the Co., to issue, *inter alia*, preference shares as part of the original capital and there is no provision or restriction in that respect in the articles which only provide for future issue of new shares, the Co. is entitled to exercise the powers expressly conferred on it by the Memo. and to issue part of the original capital as preference shares, without a special resolution (r). If rights are created by the articles, the Co. may by special resolution and without leave of the Court, alter them (s), except in cases otherwise provided by the Act.

The power and the duty of issuing shares is vested in the directors, subject to the regulations contained in the articles. The directors must exercise the power *bona fide* for the benefit of the Co. and not for any private benefit of their own. Thus they cannot ask applicants of shares to make payments on application and allotment, and issue shares, which they have subscribed for in the Memo., without making such payment themselves (t).

(m) *Mathelone v. Bom. Life Ass., A.I.R.* (1953) S.C. 385.

(n) (1901) 1 Ch. 228.

(o) *Andrews v. Gas Meter Co.* (1897), 1 Ch. 361.

(p) *Re Welsbach Co.* (1901), 1 Ch. 87.

(q) *Ashbury v. Watson* (1885), 30 Ch.D. 376.

(r) *Campbell v. Rolfe* (1933) A.C. 91.

(s) *Re Australian Estates Co.* (1910) Ch. 414.

(t) *Alexander v. Automatic Telephone Co.* (1900), 2 Ch. 56.

Classes of Shares

Shares may be (i) preference, (ii) ordinary, or (iii) deferred. *Preference shares* are shares which are entitled to a fixed dividend before any is paid to ordinary shareholders. They are not entitled to more than the fixed limit. They may be (a) cumulative, or (b) non-cumulative. In the first case, if the profits are not sufficient to pay the fixed dividend any year, the deficit must be made up out of the profits of the next year. It is not so in the second case. With regard to winding up, however, preference shares will rank *pari passu* with ordinary shares, unless they are made "preferential as to capital" also. In such a case, surplus capital, after payment of the debts of the Co., will be applied in paying off the preference shares first.

"Redeemable preference shares" are a class of preference shares which a Co. generally issues when it requires to raise money for the purpose of its business. Before 1936, Co.s under the Companies Act had no power to issue such shares. This power has given to Co.s to a limited extent by the amending Act of 1936. The same power, in a more elaborated form is now given to Co.s by s. 80 of the present Act (see ante). *Ordinary shares* get dividend after the fixed dividend has been paid on preference shares. "*Deferred shares*", often called "Founder's shares" or "management shares", are shares which are usually issued to promoters, underwriters and others who have helped in bringing the Co. into being. They are usually entitled to dividend only after a certain percentage has been paid to the ordinary shareholders. Extra voting and other rights are also attached to such shares. Notice that under the present Act, this class of shares is altogether abolished, so far as new Co.s are concerned (see below).

Share Certificate: A "share certificate" is a certificate issued by the Co. under its common seal specifying the shares held by any member (s. 84). Under s. 113, every Co. is bound, within three months of the allotment of shares or debentures or debenture stock and within three months of the registration of the "transfer" of any shares or debentures or debenture stock, to complete and to have ready for delivery, the certificates in respect of the same, unless the terms of issue otherwise provide. If default is made, the Co. and every officer thereof who is knowingly a party thereto is liable to a fine (upto Rs. 500 per day the default continues). "Transfer" here means a transfer duly stamped and otherwise valid. It does not include a transfer which the Co. is entitled to refuse to register and which is therefore not registered by it. The sec. further provides that if a notice has been served upon the Co., calling upon it to make good the default and the Co. fails to make good the default within 10 days thereafter, the Court may on the application of the person aggrieved, direct the Co. and any officer thereof, to make good the same, in which case the Co. or the officer will be liable for all costs as the Court may direct. Under art. 7 of Table A, a shareholder is entitled to one certificate for all his shares held by him, without payment. If he requires more, he must pay Re. 1 for each certificate. Where shares are held jointly, the Co. is bound to issue one certificate only and delivery of the same to one will be delivery to all.

Every share certificate shall be under the seal of the Co. and must specify the shares to which it relates and the amount paid up thereon. In case of loss, defacement or destruction of the certificate, a new one can be issued by the Co. on payment of fee not exceeding 8 annas and on such terms as to indemnity and payment out of pocket expenses of investigation as the directors may think fit (art. 8, Table A). The entry of the name of the applicant in the Share Register must be accompanied by a mention of the distinctive number of the shares actually allotted to the applicant.

In law, as s. 84 provides, a share certificate is *prima facie* evidence of the title of a member to those shares. In law, it is also *prima facie* evidence of the amount paid up on those shares. Against the Co., however, a certificate is conclusive evidence of both, the title and the amount paid on the share (u).

Share-warrants: A public Co. limited by shares if authorised by the articles may, with the previous approval of the Central Government, issue with respect to fully paid shares, warrants under its common seal, stating that the bearer of the warrant is entitled to the shares therein specified (s. 114). The sec., under the term "share warrant",

includes "stock warrant" also (see art. 39, Table A). The power to issue share warrants, payable to bearer, is denied to private Co.s. A Co. may provide by coupons or otherwise for payment of future dividends on the shares included in such warrants. Such warrants entitle the bearer thereof to the shares therein specified and the shares may be transferred, simply by delivery of the share warrant (s. 114). On the issue of the share warrant, the Co. shall strike out from its register of members, the name of the person to whom the warrant is issued as member thereof and in its stead, shall enter the following particulars: (i) the fact of the issue of the warrant, (ii) a statement of the shares included in the warrant, with their respective numbers, and (iii) the date of the issue of the warrant. If the Co. makes default in the above, the Co. and every officer who knowingly and wilfully permits the default, are liable to a fine (upto Rs. 50 per day). Until the warrant is surrendered, the above particulars will be deemed to be the particulars, required by the Act to be entered in the Register of members. (iv) When the warrant is surrendered, the date of the surrender shall be entered in the Register of members. Subject to the articles of the Co., the bearer of a share warrant shall, on surrender of the same to the Co. for cancellation and on paying such fees as may be fixed by the Board of the Co., be entitled to have his name entered on the Register as member of the Co. The Co. will be responsible for any loss caused to any person by entering on the Register of members the name of a bearer of share warrant for shares specified therein, without the warrant being surrendered and cancelled. If the articles permit and to the extent that they permit, the bearer of a share warrant may be deemed to be a member of the Co. within the meaning of the Act for any purpose defined by the articles (s. 115).

The distinction between share warrants and share certificates should be carefully noted: (i) the first can be issued only after the shares have been fully paid up, the latter can be issued at any stage; (ii) a share certificate is a document showing *prima facie* title to the shares represented thereby. A share warrant is the share security itself, transformed for the purpose of negotiation into a different character; (iii) a holder of share certificate is a member of the Co., a holder of a share warrant, may not be, unless the articles permit; (iv) share warrants are held to be negotiable instruments (v), share certificates are not.

Stocks: Stocks are fully paid up shares, consolidated and divided for the purpose of convenient holding into different parts. There may thus be stock of £1-7s.-3d. worth, while a share is usually of a round number. As Lord Cairns said in *Morris v. Aylmere* (w), "the term 'stock' merely denotes that the Company has recognized the fact of the complete payment of the shares and that time has come when these shares can be assigned in fragments which obviously could not be done before". A Co., by its articles, may give power to the directors to fix a minimum amount of stock which shall be transferable and restrict transfer of a fraction of that minimum, but the minimum shall in no case exceed the amount of the share for which the stock is issued (see art. 37, Table A). Stock may be registered or unregistered. In the first case, a register of stock is kept by the Co. and stock certificates (like share certificates), are granted. They are transferable by similar kind of transfer forms and the dividends are paid in the same way, and generally they have only the rights, privileges and advantages as regards dividend, voting and other matters, as the shares out of which they arose had and no others except participation in the dividend and property of the Co. and in the assets of the Co. on a winding up (art. 58, Table A). In the second case, stock warrants are issued which are transferable by bearer. Stock may be reconverted into shares and vice versa by an ordinary resolution (art. 36, Table A). Articles of a Co. which apply to fully paid up shares apply to stock (except those relating to share warrants) and "stock" and "stock holder" shall be interchangeable with "share" and "shareholder" (art. 39, Table A). Stocks can be reconverted into paid up shares of any denomination if the articles so provide (see s. 94). Under the Act, the provisions relating to share warrants (noted above) apply to stock warrants payable to bearer also (see s. 43).

(v) *Bechuanaland Exploration Co. v. London Trading Bank* (1878), 2 Q.B. 658.

(w) (1878), 10 Ch.App. 154.

Kinds of Share Capital

Under the present Act, two classes of share capital only are envisaged in case of a Co. limited by shares: (i) preference and (ii) ordinary or "equity share capital". What is "*preference share capital*" is now defined by s. 85. The definition is to apply to such shares, whether issued before or after the passing of the present Act. "*Preference capital*" is that part of a Co.'s capital which fulfils both the following conditions, viz. (i) that as regards dividends, it carries or will carry a preferential right to a fixed dividend, or a fixed rate of dividend, whether free of or subject to income-tax, and (ii) that as regards capital, it carries or will carry a preferential right, on a winding up or repayment of capital, to be repaid the amount paid up or deemed to have been paid up on such shares. It is immaterial for the above purposes whether the preference shares are or are not to be preferential as regards arrears of dividend due at the date of winding up or repayment of capital, or as regards any fixed premium (or fixed rate of premium) specified in the Memo. or articles. Under the sec., preference capital will not cease to do so, because, over and above the aforementioned rights as to fixed dividend, (i) it is given the additional right to participate with equity capital, either fully or to a limited extent, in respect of dividends. Secondly, preference capital will not cease to be so, because on a winding up, along with the right of preferential payment of paid up capital, it is given the further right to participate in the surplus (which may remain after the whole capital is paid off) along with equity capital. The present Act thus requires preference shares to be preferential not only as regards dividend, but also as regards capital, in order to be such.

"*Equity share capital*" has been defined by the sec. as "all the rest of the capital of a Co. limited by shares", i.e. all capital, other than "preference capital" as defined above. The Act further goes on to provide by s. 86, that the share capital of a Co., limited by shares, which is formed, after the passing of the Act or which issues capital after that date shall be of two classes only (i) equity share capital and (ii) preference share capital. This definition and classification of a Co.'s share capital has the effect, as regards new Co.s and new issues, of eliminating the deferred class of shares altogether so far as Company Law and administration in India is concerned. Notice, however, that as s. 90 provides, the above rules do not apply to private Co.s unless subsidiaries of public Co. The above division of share capital into "preference" and "equity" share capital has been introduced for the first time by the present Act. The abolition of deferred shares, which is also introduced for the first time by the present Act, has no counterpart in English Law under the Act of 1948.

Member or Shareholder

Anyone can become shareholder of a Co., e.g. a bankrupt, an alien or an infant (x). A minor, however, can repudiate the contract to take shares on attaining majority (y). An incorporated Co. can also become a shareholder (see s. 187). A firm however cannot be registered as a holder of shares; the shares must be held by the partners in their individual names (z). A person can become a "member" or "shareholder" of a Co. in any one of three ways: (i) As s. 41 provides, the *subscribers to the memorandum* of a Co. are deemed to have agreed to become members of the Co. for the shares subscribed for by them, as appearing from the Memo. and shall on registration of the Memo., be entered as members on the register of members. (ii) As the same sec. provides, every other person who agrees to become a member of a Co. and whose name is entered in its register of members, shall be a member of the Co. This comprises two classes: (a) persons who are members because they have *applied for shares*, which have then been allotted to them and (b) persons who have taken a *transfer from a member*.

Subscribers to Memo.: As to class (i), i.e. subscribers to the Memo., they are members of the Co. without more. Mere subscription to the Memo. is enough to make them members, and neither allotment nor entry in the Register of members is necessary (a). In an Allahabad case, a person had subscribed to the Memo. of association,

(x) *Re Laxon and Co.* (1892), 3 Ch. 555.

(y) *Jaffer v. Credit Bank*, 39 Bom. 331.

(z) *Ganesh Das v. R. G. Cotton Mills Ltd.*, A.I.R. (1944) Oudh 318.

(a) *Tuffnell's Case*, 29 Ch.D. 421; U.P. Oil Mills v. Jamna Prasad, 55 All. 417.

before it was filed, for a certain number of shares, but he subsequently changed his mind and asked the promoter to cancel his name and in fact, his name was not entered in the register of members. Subsequently the Co. went into liquidation. *Held*, he was liable as contributory to make good the value of the shares for which he had signed (aa).

Shareholders by Allotment: As to class (ii), i.e. shareholders by allotment, an agreement to take shares coupled with registration of the name in the Co.'s Register must be shown, otherwise the person cannot be called a shareholder. Thus in *Nicoll's Case* (b), T and P applied for allotment of shares in a limited Co. established to purchase and work a concession from a foreign Government. T and P were directors. The directors sent letters of allotment to each applicant and asked them to pay allotment moneys by a certain day. The names of the allottees, however, were never put on the Register nor were any allotment moneys paid or certificate of shares issued. *Held*, in a subsequent application by the liquidator to rectify the Register, that the Register could not be rectified by putting their names thereon, as registration, which was a condition precedent to such membership, was absent in their case. Similarly, there must be an agreement to take shares, before a person can be validly called a shareholder or member of a Co. Neither allotment nor registration of name as member in the Co.'s Register will make a person a shareholder, if there is no valid agreement to take shares. In this connection it should be observed that the principles of the law of contract as to proposal and acceptance apply to shares and the contract to take shares is not completed till the fact of allotment is communicated to the applicant. In *Pellet's Case* (c), P applied for 50 £10 shares of a Co. on the faith of an agreement with a director that he would receive orders from the Co. to the extent of £1,000, that only 30s. per share will have to be paid by him and the rest will be set off against the value of the goods supplied by him. P paid 10s. deposit on each share. The board of directors subsequently ratified the agreement. P thereafter wrote to the secretary declining to take the shares. The Co. went on asking for call money. No letter of allotment was issued but P was put on the Register. The Co. subsequently went into liquidation. *Held*, P was not a contributory, the agreement as to set off was "ultra vires" the directors, also, that by the Co. going into liquidation, the agreement, even if valid, had become incapable of fulfilment and lastly, that the contract to take shares was not complete till the fact of allotment was communicated to the defendant.

Shareholders by Transfer: As regards class 2(b), i.e. shareholders by transfer, notice that by merely obtaining a transfer of shares, the transferee does not become a member or shareholder. As was pointed out in *Fazal v. Mangaldas* (d), delivery of share certificates with blank transfer forms, passes, not property in the shares, but a title, legal and equitable, which will enable the holder to vest himself with the shares, without the risk of his title being defeated by the registered owner or any person deriving title through him. The transferee's title, as regards the Co., is not complete till his name is actually put on the Register of members.

Transmission of Shares: A share may be transferred by transmission also, i.e. by the death or insolvency of a member, when the transfer takes place by operation of law. With regard to such transmission in absence of anything to the contrary in the articles, the following rules laid down by Table A prevail: (i) Where a member was a sole holder, his legal representatives and when he was a joint holder, the survivor or survivors will be regarded as the only persons having title to the shares. This of course, does not release, in case of joint holding, the estate of the deceased from any liability to the Co. (art. 25). (ii) A person becoming entitled to a share on the death or insolvency of a member, on production of satisfactory proof as to his title may elect either (a) to register himself as holder or (b) to transfer the share as the original member could have done. In either case, the Board shall have the same powers to decline or suspend registration as in the case of the original member (art. 26). If the person concerned elects to become a member, he shall send a written and signed notice to the Co. notifying his election. If he elects to transfer, he shall notify election by executing a transfer. All rules with regard to right to transfer and registration of transfer shall apply to such notice and transfer (art. 27). (iii) A person becoming entitled to a share

(aa) *Re Chandler*, 48 All. 580.

(b) 22 Ch.D. 421.

(c) 2 Ch. 527.

(d) 23 Bom. L.R. 1144.

on transmission shall have the same right as to dividend and the other advantages and privileges as if he was the original holder, except that before registration as member, he shall not exercise any right as member at meetings of the Co. The Board may at any time give notice to such person requiring him to make his election as above and if he does not comply with such requisition within 90 days, the Board may thereafter withhold payment of all dividends, bonus, and other money to him till the requisition is complied with (art. 28).

Termination of Membership: A person, who is a member of a Co. can cease to be a member only in the following ways: (i) by transfer, which is duly registered (but with a liability to be put on the B list of contributories, see seq.); (ii) by insolvency (but his estate remains liable for amounts unpaid on the shares); (iii) by death (with the same qualification); (iv) by winding up of the Co. (in which case he becomes a contributory); (v) by valid forfeiture, (vi) valid surrender, or (vii) by sale by Co. under its lien, or (viii) by valid rescission of contract to take the shares. Similarly, a shareholder cannot get rid of his liability for payment of the amount due on the shares held by him, except (i) by payment at proper time, (ii) by transfer of the shares to another person which is duly registered, provided the Co. does not go into liquidation within 12 months thereafter, (iii) by *bona fide* forfeiture or surrender, and (iv) by reduction of the Co.'s capital. If a person deceitfully personates as the owner of a share or any interest therein, or of any share warrant or coupon attached to it and thereby obtains or attempts to obtain any such share, interest, warrant or coupon or receives or attempts to receive any money thereunder, he is liable to imprisonment (extending upto 3 years) and fine (s. 116).

Transfer of Shares: How Effectuated

The right to transfer shares is conferred by Statute. It is an absolute right, which cannot be taken away by any provisions in the articles. A shareholder can, if he so chooses, transfer his shares to a man of straw, even while the Co. is in difficulties, with a view to avoid liability thereon, if possible. An article absolutely restraining transfer would be bad and "ultra vires" the Co.

The form of transfer and the method of transfer are generally prescribed by the articles. The form of transfer given in art. 20 of Table A or a similar form may be used. A transfer must be in writing duly stamped and executed by the transferor and the transferee. This is because s. 108 provides that it shall not be lawful for a Co. to register a transfer of shares or debentures of the Co., unless a proper instrument of transfer duly stamped and executed by or on behalf of the transferor and by or on behalf of the transferee has been delivered to the Co., along with the relative certificates and if no such certificates are in existence, along with the relative letter of allotment. The only exception made is in the case where an instrument of transfer duly executed as above is lost, in which case, the Board of Directors, if satisfied about the same, can, on an application made in writing by the transferee (which must be stamped with the same stamp as instrument of transfer), register the transfer on such terms as to indemnity as they think fit. The sec. does not prejudice the power of the Co. to register any person as member to whom a right to the said shares or debentures has been transmitted by operation of law. Where a Co. has no share capital, reference to shares in the above, shall be taken to refer to the interest of the member in the Co. The requirement as to writing applies only to transfers by voluntary act of parties, it does not apply to Court sales (e).

When is the transfer of a share complete? Shares are "goods" within the meaning of the Contract Act and therefore a transfer, e.g. a sale of shares, is complete when possession of share certificates together with a transfer duly signed by the registered holder is handed over by the vendor to the purchaser. As the Privy Council said in a Bombay case, "a contract for sale of shares generally in a particular Co., without specification of their serial numbers becomes complete under s. 78 of the Contract Act (corresponding with s. 20 of the Sale of Goods Act), upon delivery to the purchaser of share certificate and the relative transfer, duly signed by the registered holder and the pur-

chaser on his part accepting the shares thus ascertained and paying for them". This is so, even though the Co. by its articles provides that only a shareholder registered as such in its books, shall be considered by it as the owner of the shares. The reason is that the documents carry with them the right and title to be registered as the owner of the shares in the books of the Co. which the transferee can enforce (f). The seller of a share does not impliedly undertake that he would procure registration of the transfer. It is enough if he delivers to the purchaser duly executed transfer form with the share certificate and then, till registration, he will be a trustee of the share for the buyer (g).

Blank Transfers: Sometimes shares are sold by handing over to the purchaser the share certificate and a "blank transfer" form. In such cases, the transfer form is signed by the transferor but the name and signature of the transferee is left blank. The advantage of this is that it saves the trouble of having a new transfer form signed by the purchaser, every time the shares pass from one hand to another by sale. The buyer either fills in his own name on the transfer form or without doing so, resells the shares and hands the blank transfer to the new purchaser, who again either inserts his own name as the transferee or resells and delivers the transfer in blank to the purchaser from him and so on. Ultimately when the shares get into the hands of a purchaser who does not want to sell them, he fills up the form by signing his own name as transferee and sends the completed transfer form to the Co. for registration. On such registration, he will be recognised as a shareholder by the Co., the other intervening parties being not such shareholders but only having had an equitable right in themselves, if they had so desired, to be registered as shareholders of the Co. As was pointed out in *Fazal v. Mangaldas* (h), delivery of the share certificates with transfer forms executed in blank, does not invest the holder of the certificates and transfer forms with the ownership of the shares in the sense that no further act is required to perfect his right. The transferor continues to be the shareholder recognised by the Co. "The delivery of share certificates with the transfers executed in blank" said Lord Watson in *Colonial Bank v. Cody* (i), "passes, not the property in shares, but a title, legal and equitable, which will enable the holder to vest himself with the shares, without the risk of his right being defeated by the registered owner or any other person deriving title from the registered holder".

Sometimes shares are mortgaged also in the same way, i.e. by depositing with the mortgagee the share certificates and blank transfer forms relating to the same. In such a case, if the amount advanced is not paid by the mortgagor at the agreed time, the mortgagee may either sign his own name as transferee on the blank transfer form and get himself registered as shareholder or may sell off the shares on the market, by handing over to a purchaser the share certificate and blank transfer. This kind of mortgage, however, is not at all safe, as the mortgagor can always get a new share certificate from the Co. by fraudulently representing to the Co. that the original is lost, and then negotiate the same for value. The danger is also not removed, by the mortgagee giving notice of the mortgage to the Co., because Co.s are not bound to recognise any trust or other equities attaching to shares (see s. 153).

If there are several transfers in respect of a share and none of them is registered, the first in time will have priority (j). But a subsequent transferee will get priority by earlier registration and that priority will not be lost because some detail remains to be done by the Co., if it is such a detail as the Co. is bound to carry out.

If a transfer is forged and the Co. registers the transfer and gives a certificate to the transferee, the true owner is entitled to sue the Co. to be put back on the Register. The Co. is not liable in damages for putting a false name on the Register but if the Co. issues a certificate on a forged transfer and somebody is damaged by acting on the faith of such certificate, the Co. is liable (k). If the transfer turns out to be invalid, the transferor remains liable for calls on the shares (l).

(f) *Bharucha v. Vadilal*, 28 Bom. L.R. 777.

(g) *Savanmal v. Shivcharan*, A.I.R. (1924) Lah. 173.

(h) 46 Bom. 489.

(i) (1890), 15 App.C. 267.

(j) *Pcat v. Clayton* (1906), 1 Ch. 659.

(k) *Bloomenthal's Case* (1897) A.C. 156.

(l) *Addison's Case* (1870), 5 Ch.App. 294.

If the share certificate relating to the share transferred, states that the share is fully paid up, that will operate as an estoppel against the Co., as against a transferee who took the share without notice that it was not fully paid up (m). Specific performance of a contract to transfer shares may be decreed, unless the directors refuse to register the transfer. In the last case, damages can be recovered. Transfer of shares during winding up is bad, unless sanctioned by the Court or the liquidator (see s. 536).

Registration of Transfers: A transfer of shares is not complete, as far as the Co. is concerned, till the transfer form duly stamped and executed by both the transferor and the transferee has been lodged with the Co. and the Co. has duly registered the transfer. In this connection s. 110 provides that an application for the registration of a transfer can be made either by the transferor or the transferee. Where, however, the application for registration of a transfer is made by a transferor and the share is partly paid up, the sec. requires that the Co. must give notice of the application to the transferee before registering the transfer and if within two weeks of the receipt of notice, no objection is made to the Co. by the transferee, then alone the Co. should register the transfer. Once a transfer is lodged with a Co., the Co. should not unduly delay the registration thereof. If the Co. is guilty of undue delay in registering a transfer, the Court would put the transferee in the same position as if there had been no delay, e.g. will treat him as a shareholder, in spite of the fact that the transfer is not registered and his name does not appear on the Register.

Refusal to Register Transfer

Articles generally give a discretion to directors to refuse to register a transfer of any share or interest therein or of any debenture of the Co. This right is recognised by s. 111(1) of the Act. The following rules are laid down by the sec., for exercise of the right of refusal to register a transfer or transmission: (i) Where a Co. refuses to register transfer or transmission in pursuance of its power in that behalf, it must send notice to the transferee or the person giving intimation of the transmission, of such refusal within 2 months of the delivery of the transfer or intimation of transmission to the Co. In case of default, the Co. and officer in default is liable to a fine (upto Rs. 50 per day) the default continues. (ii) The transferor or transferee or the person giving intimation of the transmission, can also, in case of a public Co. (or a private Co. which is subsidiary of a public Co.), *appeal to the Central Government* against such refusal to register a transfer and also where the Co. has failed to register the transfer within the aforesaid period of two months or has failed to send notice of refusal within the said period. The time for appeal against refusal to register is within two months of receipt of notice of refusal, and in the remaining cases, within 2 months of the expiry of the period mentioned in (i) above. The Central Government shall after reasonable notice to the Co., the transferor and the transferee and after giving them reasonable opportunity to make representation in writing, order either that the transfer be registered or not registered and may also make such order as to costs and other incidental matters as it may think just. The Co. shall be bound to carry out the order. Proceedings in appeal are confidential and no suit or other proceeding shall lie for any allegation made, orally or otherwise, therein. In case of a private Co. (not being a subsidiary as above), also, where right to shares or debentures therein is transmitted by Court sale or by sale by other public authority, the same provisions as above apply except that instead of the order for registering the transmission, the Central Government may direct that any member of the Co. may purchase the said shares or debentures at a price and within the time mentioned in the order.

Discretion Regarding Refusal to Register: Rules with regard to the exercise of the directors' discretion regarding refusal to register a transfer are as follows: (i) the directors in exercising their discretion to refuse to register a transfer of shares or debentures are not bound to assign any reasons for their refusal; (ii) the directors must act in good faith in the interest of the Co. and must fairly consider the question of the fitness of the transferee at a board meeting; (iii) if they exercise their power dishonestly or capriciously or from an evil motive, the Court will interfere (n). The reason is that

(m) *Burkenshaw v. Nicolls* (1878), 3 App. C. 1004.

(n) *Re Ceylon Produce Co. Ltd.* (1893), 7 T.L.R. 692.

this discretionary power of the directors to approve or reject a transfer is of a fiduciary nature and must be exercised by them in good faith (o).

The power must, in fact, have been actively exercised by the directors on whom it is conferred. In a case where an executrix of a deceased member applied for rectification of the Register by having her name substituted on the Register in place of the deceased and by the articles, the directors had absolute discretion to refuse to register a transfer, but the directors being two, were equally divided as to substitution, it was held that the power of refusal to register must be actively exercised and there being no such active refusal, the executrix was entitled to the rectification (p). It has been recently held in Madras that directors act within their powers when they refuse to register the name of a person whose character is such as to throw the affairs of the Co. into confusion and who is therefore not a desirable person (q).

Certification of Transfer: Sometimes, a shareholder who is a holder of a large number of shares, desires to sell only a part of them. In such a case he hands over to the Co., the original share certificates for the whole amount of his holding and a duly executed transfer form for such lesser amount thereof as he desires to sell. The Co. then stamps the transfer (which is for the desired lesser amount), with the original amount of the transferor's holding, e.g. "500 shares have been lodged in the Co.'s office" (the sale desired being of 100 shares thereout). This is called "*certification of transfers*" and the transfer is called "*certificated transfer*". The Co. then prepares two new share certificates, one for 400 shares which is handed over to the transferor and one for 100 shares which is handed over to the transferee, the original share certificate for 500 shares being kept by the Co. with itself for cancellation. The importance of issuing "*certificated transfers*" in this way is that such transfers are accepted on the stock exchange as a valid tender of the proper share certificates. S. 112 of the Act makes the following provisions with regard to the subject: (i) the certificate of a transfer by a Co. only amounts to a representation by the Co. to persons acting on the faith thereof, that documents have been produced before the Co. which on their face show a *prima facie* title to those shares or debentures in the transferor. (ii) It is not a representation that the transferor has any title to the shares or debentures in question. (iii) If such certificate is made by the Co. negligently, the Co. shall be liable to the person acting on the faith thereof as if it had been made fraudulently. (iv) A transfer is "*certified*" when words "*certificate lodged*" or other words analogous thereto, appear on the transfer. (v) "*Certification*" shall be deemed to be made by the Co. if (a) the person issuing the certificated instrument is authorised by the Co. in that behalf and (b) if the certification is "*signed*" by an officer, or servant of the Co. authorised in that behalf. If a body corporate has been so authorised, any authorised officer or servant of the Co. can "*sign*". "*Certification*" shall be deemed to be "*signed*" by any person, if it purports to be authenticated by his signature. If it is shown, however, that the signature is not his or was put by any person not authorised by him for purpose of certifying the transfer, the certification shall be void. In other words, a forged signature is no signature.

Calls

The amount remaining unpaid after the amounts payable on application and allotment have been paid, is generally called up by the Co. by making "*calls*" on its shareholders from time to time as necessity requires. Sometimes shares are offered with a certain amount as payable on application, a certain amount as payable on allotment and a certain other amount as payable "*after a fixed period*". The last is not a "*call*", according to the better opinion. A call must be made in accordance with the articles. In order to make a valid call, there must, in the first place, be a resolution of directors. There cannot be such a thing as making calls, without a resolution. The resolution must state the time and place of payment. If this is not stated by the resolution, the resolution is defective and the call made thereon invalid. In a Bombay case, the resolution of a board of directors of a Co. omitted to state the amount of call, as well as the

(o) *Re Beda Steamship Co.* (1917), 1 Ch. 123.

(p) *Re Hackney Pavilion Ltd.* (1924), 1 Ch. 276; *Moodec v. W. J. Shepherd Ltd.*

(1949), 2 All E.R. 1044 (H.L.).

(q) *Muthappa v. Salem Mills Ltd.*, A.I.R. (1955) Mad. 665.

time and place and person to whom the call was to be paid. *Held*, the call was bad and the defect cannot be cured by subsequent issue of notice, stating the above particulars (r). Note, however, that a subsequent resolution of directors fixing the time and place of payment of call, will validate the call as from the date of such last resolution (s). Both the amount of call, as well as the time for payment thereof, must be mentioned in the Directors' resolution making a call; otherwise the call will be invalid (ss).

S. 91 now provides that calls made after the commencement of the present Act must be made on a uniform basis as regards shares of the same class. Shares of the same nominal value, however, on which different amounts have been paid up, are not to be regarded as of the same class. A Co. has power under s. 92 to accept from a member, if so authorised by its articles, any amount remaining unpaid on shares, in "advance of call". Such advance payment however in case of limited Co.s is not to give to that member any excess as to voting rights, till such amount has been called up as regards other shareholders also. Such payment is called "*payment in advance of call*". In regard to moneys so paid in advance, the shareholder becomes a creditor of the Co., so far as interest thereon is concerned. Therefore if there are no profits, such interest may be paid out of capital. The Co. may also, if authorised by its articles, pay dividend in proportion to the amount paid up on each share, when larger amount has been paid on some shares than on the others (s. 93). Articles generally provide that a call shall not exceed in amount a certain percentage, e.g. one-fourth of the nominal value of the share, at any one time. Calls cannot be made till the "minimum subscription" as fixed by the articles has been paid. Calls must be paid in cash, unless some amount is due from the Co. to the shareholder, e.g. for services, in which case they might be set off. Note, however, that after winding up, no set-off against calls can be allowed. On a transfer of shares, the transferee is bound to pay all future calls and must indemnify the transferor against the same. If the call is made before the transfer but is payable after the transfer, it appears that the transferor is bound to pay the same (t). A call can be paid in money or money's worth. If, however, the consideration is found illusory, it would not be regarded as valid payment (u).

Dividends

"Dividends are the profits of a trading Co. divided amongst its members in proportion to their shares." The power to declare dividends is inherent in every Co. It need not, therefore, have been given expressly by the Memo. or the articles. As reg. 85 of Table A provides, the Co. in general meeting may declare dividends but no dividends shall exceed the amount recommended by the directors. The articles usually provide for the proportion in which the profits of an undertaking are to be divided each year amongst the shareholders. Where a larger amount is paid up on some shares than on others, a Co. may pay larger dividend with regard to such excess payment, if authorised by its articles (s. 93). In absence of such article, however, reg. 88 of Table A provides that, subject to the right of persons with special rights as to dividend, dividends shall be declared and paid according to the amounts paid up or credited as paid up on shares. Where no payment on shares has been made, however, dividend can be declared and paid according to the nominal amount of shares. Payment in advance of call shall not rank for dividend. Dividends shall be apportioned and paid proportionately on the amounts paid or credited as paid during the period to which the dividend relates. The Board may deduct from the dividend all sums of money previously payable for calls or otherwise in relation to the shares of the Co. (reg. 89).

Shareholders, however, are not entitled to insist on payment of a dividend, if the directors decline to declare any, however great the profits may be, except in the case of fraud. How much out of the profits of the Co. during a particular year should be used for distribution as dividend, depends almost entirely on the articles of the Co. and the

(r) *Pioneer Alkali Works v. Amiruddin*, 28 Bom. L.R. 411; *Bhagirath Sp. & W. Co. v. Balaji*, 54 Bom. 178.

(s) *Johnson v. Lyttles Iron Agency* (1840) M. & W. 243.

(ss) *East and West Ins. Co. v. Mrs. Kamala*, 58 Bom. L.R. 660.

(t) *Taylor's Case* (1897), 1 Ch. 298.

(u) *Rc White Star Line* (1938), 1 All E.R. 607.

terms of issue of various kinds of shares. Declaration of dividend, however, is a condition precedent to any claim for dividend, e.g. even in respect of shares for which the dividend is fixed by the articles, e.g. fixed cumulative preference shares (v).

The articles generally provide that dividends are to be paid by the directors with the sanction of a general meeting. But the directors can declare "*interim dividends*" also (reg. 86 of Table A). "*Ad interim*" dividend is a dividend declared in between two general meetings. The declaration of a dividend creates a debt from the Co., for which a shareholder is entitled to sue and limitation would run in favour of the Co. from the date of the declaration. No dividend can bear interest against the Co., unless the articles so provide (reg. 94, Table A).

Under s. 205, dividend can only be paid to the registered holder of the share or his order or his banker. In case a share warrant has been issued under s. 114 (*ante*), it can be paid to the bearer thereof. Notice that bankers of a registered shareholder are not required to make a separate application. Under s. 207, where a dividend has been declared by the Co. but it has not been paid or if warrant in respect thereof is not posted to the shareholder entitled thereto, within 3 months of the declaration of dividend, every director, managing agent, secretaries and treasurers (and where managing agent is a firm or corporate body, every partner and director thereof, and where secretaries and treasurers are a firm or a corporate body, every partner and director thereof), who is knowingly party to the default shall be liable to punishment of imprisonment upto 7 days and also to a fine. No offence shall be deemed to have been committed under the sec. if (i) dividend could not be paid by reason of operation of law of insolvency, (ii) where directions given by shareholder as to payment cannot be carried out, (iii) where there is a dispute as regards title to the dividend, (iv) where dividend has been lawfully adjusted by the Co. against any sum due by the shareholder to the Co., (v) where failure to pay or post the warrant as laid down by the sec. was not due to any default on the part of the Co. Unless the articles otherwise provide, dividend belongs to the party who was the owner of the share at the time it was declared, though payment thereof may have been postponed (w).

Certain important rules are to be observed with regard to dividends: (i) dividends can only be paid out of profits and (ii) they cannot be paid out of capital. This has now been statutorily provided by s. 205 of the Act, which lays down that no dividend shall be declared or paid except out of the profits of the Co., or out of moneys provided by the Central or State Government in pursuance of guarantee given in that behalf. The only exception to this rule is under s. 208 where shares are issued by a Co. for raising money to defray the expenses of any work or plant, then, with the sanction of the Central Government a Co. may pay "interest" out of capital, even though there is no profit (see *seq.*). It is often difficult to decide whether a particular item in the Co.'s account should go to the capital or to the profit (or revenue) account. Capital is of two kinds: (i) circulating capital, i.e. "property acquired or produced with a view to resale or sale at a profit", and (ii) fixed capital, i.e. "property acquired and intended for retention and employment with a view to profit" and the rule is that loss of circulating capital must be accounted for before the profits can be ascertained. On the other hand, the loss of fixed capital, e.g. by depreciation (which is usually provided for by a sinking fund) need not be necessarily or always written off, before profits are divisible amongst the shareholders (x).

Payment of dividend out of capital is "*ultra vires*", even if sanctioned by the Memo. or the Articles (y). Directors who are guilty of such payment are jointly and severally bound to repay the amount to the Co. (z). Improperly paid dividends can be recovered by the liquidator in winding up from the directors although the creditors have been paid. *Re National Bank of Wales Ltd.*, (1899) 2 Ch. 629.

(v) *Bond v. Barrow Haemetite Steel Co.* (1902), 1 Ch. 353.

(w) *Re Kinder* (1929), 2 Ch. 121.

(x) *Lee v. Neuchatel Asphalt Co.* (1887). 41 Ch.D. 1; *Verner v. General Commercial*

Trust (1894), 2 Ch. 268.

(y) *Foster v. New Trinidad Lake etc. Co.* (1901), 1 Ch. 208.

(z) *Flitcroft's Case* (1882), 21 Ch.D. 519.

The third rule about dividends is that dividends must be paid in cash and a shareholder is not bound to accept other shares or debentures in lieu thereof, unless there is an express agreement to that effect.

A transfer of shares, after dividend is declared, does not as against the Co., carry the dividend, even where the transferee has expressly bought "cum dividend". As between the buyer and seller of shares, however, the buyer is entitled to all dividends declared after the date of the contract for sale, unless otherwise arranged (a).

Capitalisation of Profits: Profits may be capitalised, i.e. instead of distributing them as dividends, they may be turned into shares, which are then given as bonuses to shareholders in proportion to their holdings, if the articles so provide. The Co., in such a case, will declare a dividend or bonus, out of its distributed profits and at the same time, issue a corresponding number of new shares, then it will apply the dividend or bonus, which belong to the shareholders, in payment of the amount due on those shares, and the shares will then belong to the shareholders as fully paid-up shares. The Co. will in this way, capitalise its profits, i.e. increase its capital by the issue, out of profits, of further new fully paid-up shares, and the shareholders will get their dividends but in the shape of more shares. This is the only case in which a Co. can issue "bonus shares". This is sometimes done without taking the intermediate steps, by the Co. issuing fully paid-up bonus shares direct.

Power to Pay Interest Out of Capital: Under sec. 208, where shares are issued by the Co. to defray expenses of construction of a work or building or the provision of any plant which cannot be made profitable for a lengthy period, the Co. can pay interest on paid-up capital on such shares and charge the same to capital, as cost of construction of work, building or plant, subject however to the following conditions: (i) the payment must be authorised by the articles or by a special resolution; (ii) in both cases, sanction of Central Government should have been previously obtained. Before granting sanction, the Central Government may appoint a person to inquire and report to the Government on the subject at the cost of the Co. and may require security from the Co. for the costs of the investigation. The grant of the sanction shall be conclusive evidence that the shares in question have been issued for the purpose mentioned by the sec. (iii) Interest shall be paid only for such period as the Central Government sanctions and in no case shall it extend beyond close of half year next after the half year in which the construction, building or plant has been completed; (iv) the rate of interest shall not exceed 4% or such other rate as notified by Central Government in Official Gazette; (v) payment of interest shall not operate to reduce the amount paid up on the shares; (vi) sec. does not affect Co.s governed by the Indian Railway Co.s' Act of 1885 and Indian Tramways Act of 1902.

Lien

Articles usually provide that a Co. shall have a "first and paramount" lien on the shares of its members for debts and liabilities due by the shareholders to the Co. The lien is either confined to partly paid shares or extends to fully paid shares as well. The Co. thereby obtains a charge on the shares held by a shareholder for debts due by him to the Co. The lien is not a possessory lien, but creates an equitable charge, which is assignable (b).

Forfeiture

The directors have no right to forfeit shares unless such power is given to them by the articles. The reason is that every forfeiture and cancellation of a share, amounts to a reduction of the capital of the Co. and this cannot be done except in the cases specified and in the manner laid down by the Act. The power to forfeit shares in the articles is usually restricted to forfeiture for non-payment of calls. Shares are also made liable to forfeiture for non-payment of any sum which by the terms of issue of a share, is made payable "after a fixed time", whether on account of the amount of the share or by way of premium. Shares cannot be forfeited, except for the reasons

(a) Chunilal Patel v. Adhyaru, A.I.R. (1956) S.C. 655.

(b) Everett v. Automatic Weighing Machine (1892), 3 Ch. 506.

mentioned above. Any article which provides that shares will be liable to forfeiture for causes other than above, is invalid and "ultra vires" the Co. The power to forfeit is in the nature of a trust and the directors must exercise it *bona fide* and for the benefit of the Co. If they do not exercise the power for the benefit of the Co., the forfeiture will be set aside.

Forfeiture is in the nature of penalty but the Court will not relieve against it, if it is duly and *bona fide* declared. But no forfeiture can be valid unless every condition necessary for its exercise has been strictly and literally complied with (c). If the power of forfeiture is wrongly exercised, the shareholder may bring an action for an annulment of forfeiture. If by reason of re-allotment of the shares, it is no longer possible for the Co. to reinstate the shareholder, he can still sue the Co. in damages (d). After the forfeiture, the Co. cannot sue the shareholder for unpaid calls unless the articles give it the power to do so. If they give such power, the ex-shareholder will be liable as an ordinary debtor and not as a contributory (e).

Surrender: Though the Indian Companies Act and Table A recognise forfeiture of shares, they make no provision for surrender of shares by a shareholder to the Co. A surrender of shares, however, is recognised by law, the one and only condition being that the circumstances must be such as would justify a forfeiture. In all other cases, a surrender of shares by a holder to the Co. is invalid. The reason is that every surrender of a share by a holder to the Co. amounts, indirectly, to so much reduction of the capital of the Co., which under the Companies Act is strictly prohibited except in the manner and under the circumstances mentioned in the Act (f).

Voting Rights

Voting rights of shareholders of each class are now no longer left to the tender mercies of Co. promoters and organisers but are statutised. Under s. 87: (i) every holder of equity share shall have a right to vote, with regard to such capital, on every resolution placed before the Co.; (ii) on poll, the voting right shall be in proportion to the amount paid up on his shares. (iii) Every holder of preference share capital shall have in respect of such capital, a right to vote only on resolutions which directly affect rights attached to the preference shares. A resolution for winding up or repayment or for reduction of share capital shall be deemed to be one affecting directly the rights of preference shareholders. Where preference shares are cumulative as to dividend and such dividend has remained unpaid for an aggregate period of two years before the date of any meeting of the Co., the preference shareholders shall have a right to vote on every resolution placed before the meeting. Where preference shares are not cumulative as to dividend, their holders will have the above extended right of voting, if dividend due on such shares as remained unpaid for *not less than two years* ending with the financial year immediately preceding the commencement of the meeting, or for *not less than 3 years out of 6 years preceding the above period*. In all the above cases, the right of preference shareholders to vote on a poll, shall be in the proportion which the capital paid up on such shares bears to the total paid up equity capital of the Co. Dividend on preference shares shall be deemed to be due on the last day of the period specified in the articles or other instrument in that behalf and if no such day is specified, on the day immediately following such period. (iv) No Co. formed or issuing capital after commencement of the Act shall issue any equity share capital carrying rights as to dividend, capital or otherwise, which are disproportionate to similar rights as regards previously issued equity capital of the Co. (s. 88). (v) Where at the commencement of the present Act, it is found that any shares, by whatever name called (and not being preference shares) carry voting rights in excess of the voting rights attached to equity shares on which equal amount has been paid up, the Co. shall equalise the said voting rights within one year of the commencement of the Act. Before their voting rights are equalised as aforesaid, the holders of such shares shall not exercise in respect thereof, voting rights in

(c) *Johnson v. Lyttle's Iron Agency* (supra); *Pramila Devi v. People's Bank of N. India, A.I.R. (1938) P.C. 284*.

(d) *Re Chili Gold Mining Co. (1890)*, 45 Ch.D. 598; *Balvant Gopal v. Ceramic Industries (1950) Nag. 150*.

(e) *Ladies Dress Ass. v. Pulbrook (1900)*, 2 Q.B. 376; *Habib Ravji v. Standard Aluminium etc., 27 Bom. L.R. 1528*.

(f) *Bellerby v. Rowland and Marwood S. S. Co. (1902)*, 2 Ch. 14.

excess of those of holders of the equity capital on which an equal amount has been paid up, in connection with the following resolutions: (i) resolution re: appointment of a director or managing agents or secretaries and treasurers or re: variation of the terms of agreement between the Co. and a managing or whole time director thereof or the persons abovementioned; (ii) resolution re: appointment of buying or selling agents; (iii) resolution re: grant of loan, guarantee or other financial assistance to any other corporate body whose managing agent or secretaries and treasurers are also the managing agent, secretaries and treasurers of the Co. or any "associate" thereof. (vi) If within one year, voting rights of any class of shareholders are not equalised as aforesaid on account of difficulty of agreement in regard to such equalisation, the Co. shall apply to Court within one month of expiry of the aforesaid period, for an order as to how the said equalisation shall be carried out. An order made by the Court on such application shall be binding on all shareholders. Default in making such application makes the Co. or officer in default liable to fine (upto Rs. 1,000). (vii) The Central Government may exempt any Co. from liability to effect such equalisation of voting rights (either wholly or partly) if it is necessary in public interest or in the interest of the Co. or any class of shareholders thereof or of the directors of the Co. or any class thereof. Exemption order of the Central Government in the above behalf must be placed before both Houses of Parliament as soon as possible after it is made (s. 89). (viii) Nothing in ss. 85-89 shall affect voting rights of shares issued before the commencement of the Act, except as provided by s. 89. (ix) The above ss. 85-89 do not apply at all to private Cos (s. 90).

ALTERATION OF SHARE CAPITAL

Varieties of Capital: Various kinds of capital have to be noted: (i) "Nominal" or "authorised capital", i.e. the nominal value of shares which the Co. is authorised to issue. It is also called the "registered capital". This must be stated in the Memo. and in the Annual Summary. (ii) "Issued capital", i.e. the nominal value of shares actually issued by the Co. for public subscription. (iii) "Subscribed capital", i.e. the total amount of the nominal value of shares which have been actually taken up, i.e. subscribed for by the public. (iv) "Called up capital", i.e. that amount of the nominal value of shares subscribed for, which the Co. has asked its shareholders to pay up by means of calls or otherwise. (v) "Uncalled capital", i.e. that portion of the nominal amount of shares issued which the company is yet entitled to call up, if it so desires, by means of calls, etc. (vi) "Paid up capital", i.e. the amount actually paid up by the subscribers on the shares issued. (vii) "Unpaid capital", i.e. that portion of the amount of the nominal value of shares which has been called up but has not been paid but is in arrears. (viii) "Reserve capital" (for which see s. 99 seq.). (ix) "Debenture capital". This, however, is a misnomer, money borrowed on debentures not being capital at all. (x) "Watered capital", also called "inflated capital", i.e. that portion of the capital of a Co. which is not represented by equivalent tangible assets, but which represents a special value which the Co. has placed on a particular item of its capital, e.g. a goodwill of a business, which the Co. has purchased. Issue of bonus shares is another illustration of the same variety of capital.

Alteration of Share Capital

S. 94 of the Act provides that a limited Co. having share capital, if so authorised by its articles, may alter the conditions of its Memo. as follows: viz. it may (a) increase its authorised share capital by such amount as it may think expedient, by issue of new shares, (b) consolidate and divide all or any of its share capital into shares of larger amounts than its existing shares, (c) convert all or any of its fully paid up shares into stock and re-convert that stock into fully paid up shares of any denomination, (d) sub-divide its shares or any of them, into shares of similar amount than is fixed in the Memo., provided, however, that the proportion between the amount paid up and that unpaid on each reduced share remains the same as before, (e) cancel shares which, at the date of the resolution in that behalf, have not been taken up or agreed to be taken by any person and thus diminish the amount of its share capital by the amount of shares so cancelled. A cancellation under this last cl. will not be regarded as reduction of share capital under the Act. The powers given by the sec. can be exercised by the Co. in general meeting and shall not require confirmation by the Court.

Increase of Capital: The power to increase share capital can be exercised by the Co. from time to time. Under s. 94, the power can be exercised by the Co., if authorised by the articles to do so. The power can be exercised by the Co. in general meeting, in the manner provided by the articles, i.e. by a special or ordinary resolution. Under the sec., similar powers are also vested in guarantee companies having share capital.

Conversion of Shares into Stock: Only fully paid-up shares can be converted into stock. Where a company purported to issue bonus stock and partly paid stock, *held*, both the issues were void and the holders had no rights and therefore no calls could be made on them (g). Notice of conversion must be given to the Registrar under s. 95. Stock warrants payable to bearer can be issued by a company under s. 114, with the sanction of the Central Government.

Sub-division of Shares: Power to sub-divide shares must be given by the articles. It must be exercised by the Co. in the manner prescribed by the articles. The proportion between the amount paid and unpaid on such shares must be maintained on sub-division. If sub-division involves a reorganisation of the different classes of shares constituting the share capital, the procedure laid down in s. 391 must be followed.

Consolidation of Shares: Under the sec., consolidation of shares can be effected by a Co. if power to do so is given by the articles. The power must be exercised by the Co. in general meeting by means of special or ordinary resolution as the articles provide. Where consolidation involves no alteration of the Memo., it can be accomplished by the appropriate resolutions and no sanction of the Court is required. Even where alteration of Memo. is involved, if the consolidation consists of amalgamation and thereafter division of shares into shares of larger amount, no sanction of the Court will be necessary as provided by the sec. Where consolidation (or sub-division), however, involves an alteration of the Memo. and further either the consolidation of shares into different classes or division of shares into different classes, with or without alteration of their respective rights, the matter will not fall under s. 94 but under s. 391 and will now have to be carried out as a scheme of arrangement (see *seq.*).

Procedure: Under ss. 95-97, the following steps are necessary: (i) Where shares are consolidated into shares of larger amounts, or converted into stock or reconverted into shares, or sub-divided or where the Co. redeems any redeemable preference shares or cancels any shares (otherwise than as on reduction of capital), the Co. shall, within one month of doing so, give notice to the Registrar specifying and giving particulars of the alteration affected. The Registrar will record the notice and make such alterations in the Co.'s Memo. or articles as may be necessary. The Co. and every officer in default, as regards the above is liable to a fine (extending to Rs. 50) for every day the default continues (s. 95). Where the Co. has given such notice to the Registrar of conversion of its shares into stock, all provisions of the Act regarding shares shall cease to apply to such stock (s. 96); (ii) where a Co. increases its share capital beyond its authorised capital and where a Co. not limited by shares increases the number of its members beyond the registered number, it must file a notice with the Registrar of such increase within 15 days of the passing of the resolution authorising the increase. The Registrar will record the increase and make the necessary alterations in the Memo. or articles or both. The notice must give particulars of the classes of shares affected and the conditions subject to which the new shares are issued or to be issued. Penalty for default is Rs. 50 per day the default continues to the Co. and officers in default (s. 97).

Reserve Capital: A limited Co. may by *special resolution* resolve that any part of its uncalled capital, shall not be capable of being called up, except in the event of and for the purposes of winding up. Such capital is called reserve capital and it cannot be called up except when the contingencies mentioned occur (s. 99, which reproduces s. 69 of the Act of 1913). According to Palmer, when once liability is so reserved, it cannot be affected afterwards by a special resolution. Uncalled capital can be charged by the Co. in respect of any proposed borrowing but once uncalled capital has been turned into reserve capital under the sec., it has been held that no charge can be created by

the Co. thereon (h). Palmer however doubts the distinction. Where an unlimited Co. having a share capital proposes to register itself as a limited company under the provisions of the Act, s. 98 (which replaces s. 68 of the Act of 1913) empowers such Co., by its resolution to so register, to provide also for (i) increase of its nominal share capital by increase of the nominal amount of its shares, subject however to the condition that such increased amount shall not be called up except in the event and for the purposes of winding up. (ii) It may also provide that a specified portion of its uncalled capital shall not be called up except in the event of and for the purposes of winding up.

Reduction of Share Capital

S. 100 provides that a Co. limited by shares or a Co. limited by guarantee and having a share capital, if so authorised by its articles, may, by special resolution, reduce its share capital in any way, and in particular (without prejudice to the generality of the abovementioned power) may, (a) extinguish or reduce the liability on any of its shares in respect of share capital not paid up; or (b) either with or without extinguishing or reducing liability on any of its shares, cancel any paid-up share capital which is lost or is unrepresented by available assets, or (c) either with or without extinguishing or reducing such liability on its shares, pay off any paid-up share capital which is in excess of the wants of the Co.; and may, if and so far as is necessary, alter its Memo. by reducing the amount of its share capital and of its shares accordingly. A special resolution under this sec. is called a "*resolution for reducing share capital*".

Thus a company can reduce a 100 Rs. share on which Rs. 75 are unpaid by writing off Rs. 50 of the unpaid amount or with or without reducing the unpaid liability, cancel any part of the paid-up capital which is lost or with or without reducing the unpaid liability, pay off its shareholders any paid-up capital which is in excess of its needs.

Procedure for Reduction of Share Capital: The procedure with regard to reduction of capital as laid down by s. 101 is as follows: (i) The Co. must first pass a special resolution for reduction of capital; (ii) the Co. must then apply to the Court by petition to confirm the reduction; (iii) every creditor of the Co. who at the date fixed by the Court, is entitled to any debt or claim which would be provable against the Co., if that date were the date of the commencement of winding up, i.e. every existing creditor of the Co., shall be entitled to object to the reduction (a) as a matter of right, where reduction involves reduction of liability on any share in respect of unpaid share capital, or repayment of amount already paid on any shares and (b) in other cases, if the Court so directs. (iv) The Court shall settle a list of such creditors who are entitled to object as above and for that purpose ascertain the names of the creditors, the amounts and nature of their claims and may publish notices, fixing a day or days within which creditors not entered in the list are to claim to be so entered or are to be excluded from the right of objecting to the reduction. (v) Where a creditor entered on such list does not consent to such reduction and his debt is not discharged or determined by the Co., the Court may, if it thinks fit, dispense with his consent, if the Co. secures payment of his debt or claim by appropriating as the Court directs, the full amount of the same, where the whole is admitted or if the Co. is willing so to do; and where a part is admitted or the Co. is not willing to provide for the whole, or where the debt or claim is contingent or unascertainable, such amount as the Court may direct after inquiry as on a winding up. The Court has discretion to direct that the above provisions shall not apply to any class or classes of shareholders, if under special circumstances it thinks fit to do so, in cases where reduction involves diminution of unpaid liability on shares or repayment of paid-up capital (s. 101). (vi) The Court will then, if satisfied that every creditor of the Co. entitled to object, has consented to the reduction or has his debt discharged or secured as aforesaid, make an order confirming the reduction on such terms and conditions as it thinks fit. The Court may at the time of confirmation, if for special reason it thinks proper, order that the Co. shall from the date of the order add to its name as last words thereof, the words "and reduced" for such time as may be specified in the order. These words are to be deemed to be part of the Co.'s name for such specified period. The Co. shall, if the Court so directs, also publish reasons for the reduction and all other

information regarding thereto, including causes for reduction for public information as the Court may direct (s. 102) (i). (vii) The order of the Court confirming the reduction must be produced before the Registrar and a certified copy thereof should be filed with him. With such copy should also be filed a minute (approved by the Court) showing, with regard to the share capital as altered by the order: (a) the amount of share capital, (b) number of shares into which it is to be divided, (c) the amount of each share, and (d) the amount (if any) at the date of registration, deemed to be paid up on each share. (viii) The Registrar then will register the order and the minute. (ix) *On such registration only, the resolution for reduction of the share capital as confirmed by the order so registered, shall take effect.* (x) Notice of registration shall be published in such manner as the Court may direct. (xi) The Registrar shall certify the registration of the order and the minute under his hand and his certificate shall be conclusive evidence that all the requirements of the Act with regard to reduction of share capital have been complied with and that the share capital is as stated in the minute. (xii) The minute, when registered, shall be deemed to be substituted for the corresponding part of the Memo. and shall be valid and altered as if it had been originally contained therein. The substitution of such minute will be deemed to be an alteration of the Memo. within the meaning of the sec. (s. 103). (xiii) If any officer knowingly conceals the name of any creditor entitled to object, knowingly misrepresents the amount or nature of his claim or abets or is privy to such concealment or misrepresentation, he will be liable to imprisonment (extending to one year) or fine or both (s. 105). Notice that unless the articles otherwise provide, the power to reduce capital subject to provisions of the Act and the terms of issue, extends not only to the share capital of the Co., but also to the "capital redemption reserve fund" and the "share premium account" of the Co. also (see reg. 46, Table A).

Liability of Members on Reduction: On and after such reduction every member of a Co., whether past or present, shall not be liable in respect of any share to any call or contribution, exceeding the difference between the amount paid (or the reduced amount deemed to have been paid) on each share and the amount of the share as fixed by the minute. But (i) if a creditor who is entitled to object to the reduction and whose claim has not been entered in the list, subsequently comes forward and proves his ignorance of the proceedings for reduction or of their nature and effect upon his own interest and the Co., within the meaning of the terms in a winding up, is "unable to pay his debt" (see s. 433), then, every person who was a member of the Co. at the date of registration of the order for reduction and minute, shall be liable to contribute for the payment of the debt or claim, an amount not exceeding the amount which he would have been liable to contribute if the Co. had commenced to be wound up the day before that registration, i.e. the full amount on his original liability in respect of his share, and (ii) if the Co. is wound up as a matter of fact, the Court, at the instance of such creditor may settle a list of members so liable to contribute and enforce calls on them as if they were ordinary contributories in a winding up.

Reduction of Capital Generally: It should be observed that it is not sufficient that the power to reduce capital is given by the Memo. (j). The articles must provide for it also. If they do not, they must be altered by special resolution which must be done before the special resolution for reduction is passed (k). Note also that a reduction of share capital by cancellation of shares which have not been taken up (under s. 94) is not really a reduction but a diminution of share capital and is not covered by s. 100. A Co. can reduce its share capital in any way that is suitable. The power of reduction given by s. 100 is general and includes every possible mode of reducing capital, provided the conditions laid down by the sec. are followed.

Variation of Shareholders' Rights

Under s. 106, a Co. having a share capital, divided into different classes of shares, may provide by its Memo. or articles, for variation of the rights attached to any class of shares, subject to the following conditions: (i) the variation must be consented to

(i) *Re Walker and Smith*, 72 L.J.Ch. 572.
(j) *Re Dexine etc. Rubber Co.* (1903), 88
L.T. 791.

(k) *Re Patent Invest Sugar Co. Ltd.*, 31
Ch.D. 166.

by not less than $\frac{3}{4}$ of the holders of the issued share capital of that class or (ii) it must be sanctioned by a resolution passed at a separate meeting of that class by holders of not less than $\frac{3}{4}$ of the shares of that class. Any provision contrary to the above, contained in any Memo. or articles of a Co. at the commencement of the Act, shall be effective, after such commencement, as if it contained the aforesaid provision. Notice that under reg. 4 of Table A, unless the terms of issue otherwise provide, rights attached to any class of shares (preference or otherwise) shall not be deemed to be "varied" by the creation or issue of further shares ranking *pari passu* therewith. Consent of shareholders should generally be in writing (reg. 3). A special resolution passed at a separate meeting of the class concerned may also be sufficient (*Ibid*). Rules of Table A as regards meetings, will apply to meetings held under the sec. with the qualification that the necessary quorum shall be two persons holding or representing by proxy one-third of the issued share capital of the class (*Ibid*). The above rules apply even where the variation is sought to be made during winding up (*Ibid*). It has been held in England that not only in case of issue of new shares but also in the case of sub-division of existing shares, no variation of rights of the existing shareholders will be deemed to have occurred thereby merely because the dividend originally paid is reduced by the change (l).

Rights of Dissentient Shareholders: Under s. 107 where rights attached to any class of shares are varied as aforesaid, then the holders of not less than 10 per cent of the issued share capital of the class who have not voted in favour of or consented to the variation, may apply to the Court to have the variation cancelled. Where such an application is made, the variation shall not take effect unless and until it is confirmed by the Court. The application must, however, be made within 21 days of the consent or passing of the resolution. It can be made by one or more members of the class objecting as may be appointed in writing for that purpose. The Court on such application will hear the applicant and any other person who applies to the Court to be heard and who appears to be interested. If after hearing such persons, the Court is of the opinion that the variation would unfairly prejudice the shareholders of the class represented by the applicant, the Court will disallow the variation. If it is not so satisfied, it will confirm it. The decision of the Court on such application shall be final. The Co. shall, within 15 days of the service on it of any Court's order on such application, forward a copy of it to the Registrar. In default, the Co. and any officers in default are liable to a fine (not exceeding Rs. 50). The sec. is an important addition to the rights of a minority of shareholders to complain and if possible, to set right, the decisions of the majority, duly arrived at, when such decisions unjustly affect their rights. The power given by the sec. is exercisable, not only when rights annexed to a particular class of shares are varied, but also when they are sought to be abrogated altogether, under a valid decision of the majority. The requisite authority of shareholders for supporting a protest under the sec. must be obtained before the petition is filed and not before the hearing of the petition (m). Further, the requisite authority must have been communicated to the applicant before the petition is filed (n). A defect in the above requirements cannot be cured by subsequent ratification (*Ibid*).

DEBENTURES

Debentures: Their Nature: The word "debenture" has not been defined by the Act. According to Palmer, the word signifies "any instrument under seal, evidencing a deed, the essence of it being the admission of indebtedness". And so it was described in *Lemon v. Austin Friar's Trust* (o) by the Court of Appeal, as "something which was a mere acknowledgment of indebtedness, without containing a charge at all". In other words, a debenture means and is nothing more than, a mere acknowledgment of a debt. It has thus been held that it need not be under seal (p). It need not fix any time for repayment of the debt. It need not contain any provision for payment of interest. It need not be more than one in number and need not also be accompanied by a trust

(l) *Greenhalg v. Ardene Cinemas* (1946),
1 All E.R. 512.

(m) *Re Suburban v. Provincial Stores Ltd.*
(1946), 2 All E.R. 521.

(n) *Re Sound City Films Ltd.* (1947) Ch.
167.

(o) (1926) Ch. 1.

(p) *British India Co. v. Comm.* (1881), 7
Q.B.D. 165.

deed. Lastly, it need not contain a mortgage or charge on any property or assets of the Co. at all. And so, the new Act provides that "debenture, unless the context otherwise requires, includes bonds and other securities of a Co., whether they constitute a charge on the Co.'s assets or not."

Form of Debentures: Debentures are in various forms and may be payable to bearer or to registered holder. Those of the first class are negotiable instruments and are, therefore, transferable by delivery (q). Debentures payable to registered holders are transferable in the manner specified in the conditions endorsed thereon. Debentures payable to registered holders are sometimes issued with "coupons", for interest attached to them. In such cases, the coupons are negotiable, though the debentures are not. Debentures often contain a bond and a charge on some portion of the Co.'s property or another, or a bond simply. In the first case, they are called "mortgage debentures", in the second case, they are called simply "debentures" and merely amount to a promise to pay. They are often issued in a "series", with a "*pari passu* clause", i.e. a clause whereby all debentures of a particular series, though issued at different and varying times, are to rank "*pari passu*", i.e. together, as regard the security created by them. If, therefore, in such a case, the security is not sufficient to satisfy the whole debt secured by the issue, the debentures will abate proportionately (r). If such words are not mentioned, the debentures would be payable according to the date of issue, or if they are all issued on the same day, then according to their numerical order. Thus where 150 debentures of £100 each bearing Nos. 501 to 650 were issued on the same day and as to Nos. 501 to 600 it was stated that the issue was for £10,000 to be paid "*pari passu*", and as to Nos. 601 to 650, that the issue was for £5,000 to be paid "*pari passu*", it was held that the first lot was to be paid before the second (s). If the first lot of debenture deeds had contained a further power to issue the second lot "*pari passu*" with the first issue, the presumption arising from the sequence of numbers would have been rebutted. Debentures also often contain the power for further issue of debentures of the same series (if necessary) upto a certain specified limit. Debentures issued under a power so reserved are also subject to the above rules. The security may be created by the debenture itself or the debenture may be secured by a trust deed accompanying it. In the first case, the conditions provide that on the security becoming enforceable, the majority of holders may enter into possession. Even otherwise, they can file a suit for possession and for the enforcement of the security and for receiver. Debentures may and often are accompanied by a trust deed conveying property as security to trustees for the benefit of the debenture-holders. A legal mortgage is thereby created and the legal estate vests in the trustees. Conditions for enforcement of security are specified in the trust deed, and if they happen, the trustees can enforce the security, take possession of and sell the same or appoint a receiver of the same. The existence of trustees also prevents a subsequent legal mortgagee from obtaining priority. Debentures are not said to be "issued" till they are delivered (t). The Co. possesses the same power to refuse to register a transfer of debentures as it does in case of shares under s. 111 of the Act, if articles give such power to the Co. It has been held in England that where a debenture is forfeited for non-payment of calls or instalments, a right to sue for arrears does not survive in favour of the Co., though articles may contain provision to keep such arrears alive as in case of shares (u).

Perpetual Debentures: The date fixed for repayment of the loan may be five, ten or any other fixed period of years. Debentures may also be issued payable on demand. Debentures may be perpetual also. This is recognised by s. 120 which provides that a condition contained in any debentures or in any deed for securing debentures, whether issued or executed before or after the passing of the Act, shall not be invalid by reason only that thereby the debentures are made irredeemable or redeemable only on the happening of a contingency, however remote, or on the expiration of a period, however long. If debentures are issued as "irredeemable" or "perpetual", there would be no time within which the Co. would be bound to pay them. This, however, does not mean

(q) Bechuana Land Exploration Co. v. London Trading Bank (1898), 2 Q.B. 658.

(r) Re Smelting Corp. (1915), 1 Ch. 472.

(s) Gartside v. Silkstone etc. Co. (1882), 21 Ch.D. 762.

(t) Mowatt v. Castle Steel etc. Co. (1886), 34 Ch.D. 58.

(u) Kaula Rubber Ltd. v. Mawbray, 111 L.T. 1072.

that the Co. can never pay them off, even if it wishes to do so. It only means that the creditor cannot, at any particular time, compel the Co. to redeem them.

Re-issuing Debentures : Debentures sometimes contain clauses entitling the Co. to keep alive and re-issue debentures which have been first redeemed by the Co. so as to rank "*pari passu*" with the original issue. S. 121 provides that where either before or after the commencement of this Act, *unless* (i) any contrary provision is contained in the articles, impliedly or expressly or in the conditions of issue or in any contract entered into by the Co., or *unless* (ii) the Co. has manifested an intention to cancel the debentures by a resolution or any other act, the Co. shall have power and always be deemed to have had the power to *keep alive the debentures* for the purpose of re-issue. In the exercise of this power, the Co. shall be deemed to have and to always have had the power to re-issue the debentures either by re-issuing the same debentures or other debentures in their place and on such re-issue, the holders of such re-issued debentures shall have and shall always be deemed to have had the same rights and priorities as if the debentures had never been previously redeemed. Where for the purpose of keeping them alive, the debentures have, either before or after the commencement of the Act, been transferred to a nominee of the Co., a transfer from such nominee shall be deemed to be a re-issue under the sec. Where before or after the commencement of the Act, a Co. has deposited debentures to secure advances from time to time on current account, the debentures shall not be deemed to be redeemed by the mere fact that the current account has ceased to be in debit, whilst the debentures remain so deposited. A re-issue of debentures under the sec., whether before or after the commencement of the Act, shall be deemed to be an issue of new debentures for the purpose of stamp duty but it shall not be so treated for the purpose of any provision limiting the amount or number of debentures to be issued. A person lending money on the security of any re-issued debenture which appears to be duly stamped may give the debenture in evidence in any proceedings to enforce the security without payment of the stamp duty or penalty in respect thereof, unless he had notice or but for his negligence would have had notice that it was not duly stamped. In any such case the penalty can be recovered from the Co. The sec. does not prejudice (i) any decree or order of Court made before the 25th February 1910 or any appeal from the same as between the parties to the same and (ii) any power reserved in any debentures to a Co., or in any security for the same, to issue debentures in place of debentures paid off, extinguished or otherwise satisfied.

Debentures Can Be Issued at a Discount : Debentures may be issued at a discount, if permitted by the articles of the Co. This is because they do not form part of the capital of the Co., money borrowed on debentures not being capital. Similarly, interest payable on debentures is a debt and may be paid out of capital. Notice that under sec. 219 debenture-holders have the same right to receive copies and inspect the balance sheets and profit and loss accounts of the Co. and the auditors' and other reports, as are possessed by the ordinary shareholders. Where there are trustees for debenture-holders they also enjoy the same right. The above does not apply to private Co.s. Debentures can be issued at any time if the Co. has power to issue debentures. On a winding up, however, the Co.'s power comes to an end. If, however, debentures are issued in series, the Co. can allot the remainder of the series, even after the debenture-holders have commenced an action to enforce the security, provided no receiver has already been appointed (v).

Voting and Other Rights of Debenture-holders : S. 117 provides that no Co. shall after commencement of the Act, issue debentures, carrying voting rights at any meeting of the company, whether generally or with regard to any special kind of business. This provision is entirely new. Under English Law, debenture-holders are not denied the right to vote, if the debenture terms give such power to them.

S. 118 further provides that every debenture-holder and member of a Co. is entitled, on application, within 7 days thereof, to a copy of the trust deed (if any) for securing the issue of debentures on payment of a fee: (if printed Re. 1 per copy, if otherwise, 6 annas for every 100 words). If such copy is refused or not supplied in time, the Co. and officer in default are liable for each offence, to a fine and a further fine per day

the default continues. The Court may also order such copy to be furnished. The trust deed shall also be open to inspection of members and debenture-holders, in the same manner and extent, and on payment of the same fees, as if it were a register of members.

Re-payment of Debentures: Debentures state the conditions on which they will be repayable. Generally it is failure to pay interest regularly, levying of distress, passing of resolution for winding up and/or appointment of a receiver. Even if there is no such condition, it has been held that debentures will be repayable on a winding up commencing (*w*). As s. 122 provides, specific performance of an agreement to give debentures may be decreed against a Co. The Co. can also specifically enforce against another an agreement to take debentures.

Registration of Debentures

It is not necessary that every kind of debenture must be registered under the Companies Act. S. 125 of the Act only provides that (a) a mortgage or charge for the purpose of securing the issue of debentures, and (b) a floating charge on the undertaking of the company, shall be void as regards the security created thereby, against any creditor or liquidator unless registered within 21 days after the date of its creation with the Registrar. The result of this is that it is only (a) mortgage debentures (including in the term, debentures creating a charge), and (b) debentures secured by a floating charge, which are compulsorily registrable under the sec. Other kinds of debentures need not be therefore registered and will be valid, notwithstanding. S. 128 of the Act further provides that where a series of debentures containing or giving by reference to any other instrument any charge, to the benefit of which the debenture-holders of that series are entitled "*pari passu*", is created by a company, it shall be sufficient if, within 21 days after the execution of the deed or if there is no deed, after the execution of any debentures of the series, there are filed with the Registrar the following particulars: (i) the total amount secured by the whole series; (ii) the date of the resolution authorising issue of the series and the date of the covering deed (if any) by which the security is created or defined; (iii) a general description of the property charged; (iv) the names of trustees (if any) for the debenture-holders: together with (v) the deed (or a copy thereof verified in the prescribed manner) containing the charge or if there is no such deed, then, one of the debentures of the series; (vi) where more than one issue is made of the debentures of the series, the particulars of the dates and amount of each issue shall be filed with the Registrar but omission to do this will not affect the validity of the debentures issued. The Registrar on payment of proper fees shall enter the particulars in the register.

Under s. 129, where commission, allowance or discount has been paid directly or indirectly by the Co. to any person, in consideration of his subscribing or agreeing to subscribe, absolutely or conditionally, or procuring or agreeing to procure subscriptions whether absolute or conditional, for any debentures, the particulars required to be filed with the Registrar shall include the amount or the rate per cent of the commission, allowance or discount. Omission to do so, however, shall not vitiate the issue. Also a deposit of the debentures as security for a debt due by the company is not an issue of debentures at a discount. Certificate of registration must be endorsed on every debenture or certificate of debenture stock (s. 133).

The Madras High Court has held that debentures secured by a mortgage of immovable property require to be compulsorily registered under the Registration Act also, if they fall under s. 17 of the latter Act (x).

Transfer of Debentures: Debentures are choses in action and are transferable in the manner laid down by the Act, i.e. by delivery, if they are debentures payable to bearer (i.e. unregistered) and by due registration of transfer, in case of registered debentures. Being choses in action, they are transferable, subject to all equities existing at the time. In order to save itself from consequences such as these, a clause is frequently introduced in the debentures whereby the Co. is allowed to disregard equities between

(w) *Re Wallace Universal Automatic Co.*
(1894), 2 Ch. 547.

(x) *Vishvanadham v. Menon*, I.L.R. (1939)
Mad. 199.

itself and the transferor. Thus in *Farmer v. Goy & Co. (y)*, the debentures contained a clause that the principal and interest secured thereby will be paid to the transferee without regard to the equities between the Co. and the transferor. A resolution for winding up was passed and thereafter a director of the Co. who was guilty of misfeasance transferred his debentures to another. *Held*, the transferee took a title free from all claims of the Co. Under s. 152, every Co. is now bound to maintain a Register and Index of debentures and to enter therein the particulars required by the sec.

Remedies of Debenture-holders

Debenture-holders desiring to realise their security can proceed to do so in any of the following ways: (i) By instituting a "*debenture-holder's action*", i.e. an action by a debenture-holder on behalf of himself and all the other debenture-holders of the Co. to obtain payment of their debts or to enforce their security by sale. The Court, in such an action, will usually appoint a receiver and if necessary for the purpose of the business of the Co., a manager also and will declare the debentures to be a charge on the Co.'s assets, direct an inquiry as to who are the debenture-holders and order a sale of the property (see below). Where the Co. has ceased to carry on business and the security is in jeopardy, a debenture-holder's action is permissible though the time for payment has not arrived (z). (ii) The debenture-holder can himself appoint a receiver, if power to that effect is expressly given by the debenture deed and if the conditions for the exercise of that power are all fulfilled. (iii) A debenture-holder may apply to the Court for foreclosure of the right to redeem. This remedy, however, is unusual and for its proper exercise, it is necessary that all the debenture-holders of the Co. (as distinguished from those of a class) should join (a). Foreclosure may extend even to the uncalled capital of the Co. (iv) He may also present a winding up petition being a creditor of the Co. for the amount advanced by him and interest thereon (see *seq.*). (v) If such a power is given by the debenture deed, he can also sell the property through the trustees. (vi) If the Co. is insolvent, he can value his security and prove for the balance or surrender his security and prove for the whole amount of his debt. If the debenture-holder owes a debt to the Co., which is unable to pay its debts in full, the holder cannot set-off his debt against the liability he owes to the Co. The rule is that a person who claims a share in a fund must pay up everything he owes to the fund before he can claim a share (b).

Priority of certain Debts over Debenture Charge: Under s. 123, where a receiver is appointed on behalf of debenture-holders secured by floating charge, or where possession is taken of any property of the Co. comprised in the charge, by such debenture-holders, while the Co. is a going concern, debts which have priority of payment on a winding up, under Part VII of the Act, shall be paid in priority to principal and interest due under the charge to the debenture-holders. In this connection provisions of s. 530 regarding payment of accrued holiday remuneration to employees of the company shall be deemed to have reference to payment accrued due on appointment of receiver or taking possession of the Co.'s property as the case may be. The periods of time mentioned in Part VII shall also be counted from the above dates. Where a receiver has been appointed or property of the Co. has been taken possession as above before the commencement of the Act, the provisions kept alive by sub-sec. (9) of s. 530 will apply in the above behalf and not the above provisions of the sec. All payments made under the above provisions shall be recouped from the assets of the Co. available for general body of creditors.

Debenture Stock

This is borrowed capital in one consolidated mass. In case of ordinary debentures, each debenture is a separate mortgage or charge in favour of each holder. To obviate the inconvenience of this, debenture stock is issued. Debenture stock is a certificate entitling each holder thereof to a certain sum which is a portion of a larger loan, for the whole of which the mortgage has been created. Debenture stock is almost always

(y) (1900), 2 Ch. 149.

(z) *Wissner v. Levison and Steiner* (1900) W.N. 152.

(a) *Wallace v. Evershed* (1899), 1 Ch. 891.

(b) *Re Brown & Gregory Ltd.* (1904), 1 Ch. 627.

accompanied by a trust deed. A debenture is a document evidencing a debt. Debenture stock is the debt itself divided into convenient parts to simplify transfer. It is evidenced by a document called "debenture stock certificate".

Register of Debentures: Under ss. 130 and 131, the Registrar is bound to maintain a register and an Index of mortgage debentures and debentures creating a charge on the Co.'s property. In case of a series of such debentures, particulars to be entered in the register must include the date of the creation of mortgage or charge, the amount secured, particulars of the property and person entitled to the mortgage or charge. The register is to be open to inspection of all persons on payment of a small fee. The Co. is also bound to maintain a similar register under s. 143. Copies of such instruments have to be kept at the Co.'s registered office and the same and the register of charges maintained by the Co. must also be kept open for inspection and for taking copies by persons under s. 144.

BORROWING POWERS

Borrowing Powers of Companies: Ss. 124-145 deal with the various rules which have to be observed by a Co. which proposes to borrow moneys on the security of its property or otherwise for the purpose of its business. Generally, every trading Co. has an implied power to borrow. In case of a non-trading Co., however, such power cannot be presumed. It must be conferred or must fairly be inferred from the language of the Memo. or articles. If there is no power to borrow given by the articles or Memo., the Co. may acquire the same under s. 31 in cases coming within the sec. If a Co. has borrowing powers, it has also impliedly the power to charge its property as security for repayment of the loan. Thus in *General Auction Co. v. Smith* (c), where a Co. was formed for the purchase and sale of estates, to accept loans and deposits and the Memo. gave the Co. no power to borrow, it was held that a loan obtained by the Co. on the security of some of its land, for the purpose of paying off a deposit, was good, together with the mortgage, as the Co. was a trading company and as such had implied power to borrow and mortgage. A Co. has the same power to mortgage and sell its properties as an individual (d).

Under s. 293, the Board of Directors of a public Co. and of a private Co. which is subsidiary of a public Co., shall not, without the consent of such public or private Co. in general meeting, have power, after the commencement of the present Act, *inter alia* to borrow moneys, exceeding the paid-up capital of the Co. plus the free reserves of the Co. (i.e. reserves not set apart for any specified purpose). In fixing the above limit, at any time, moneys already borrowed by the Co. (but not including temporary loans obtained by the Co. from its bankers for purposes of its business), are to be taken into account.

If the borrowing is "ultra vires" the directors, but "intra vires" the Co., the amount can be recovered in an action for moneys had and received (e). The rule in *Clayton's Case* also will not apply to such cases, and the repayments will first discharge the "ultra vires" borrowings (*Ibid.*).

Where a Co., however, borrows without or in excess of the power conferred on it by the Memo., the borrowing is "ultra vires" the Co. and cannot be ratified by the Co. subsequently (f). The Co. cannot also make it good by extending its borrowing powers under s. 17 *ex post facto*. Securities given for such a debt will be inoperative and the lender cannot sue on the loan. According to a recent decision, however, where the moneys borrowed "ultra vires" are used in payment of valid pre-existing debts of the Co., the borrowing will not be invalid, because no new debt is thereby created and the Co.'s indebtedness is not increased. The lender will, in such case, stand by subrogation into the shoes of the creditor of the Co. who is paid off, so far as the validity of his loan is concerned (g).

(c) (1891), 3 Ch. 432.

(d) *Re Collieries* (1907), 2 Ch. 259.

(e) *Reversion Fund v. Maison Causeway* (1913), 1 K.B. 364; *Pratt (Bom.) Ltd. v. F. D. Sassoon and Co.*, 37 Bom. L.R. 978; *Re Cine Recording Co.*, 44 Bom. L.R. 34.

(f) *Re National Permanent Building Society* (1869), 5 Ch.App. 309; *Sinclair v. Brougham* (1914) A.C. 398, 440.

(g) *Reversion Fund v. Maison Causeway* (supra).

Ways of Borrowing: A Co., if authorised to borrow, can borrow moneys in such manner as it thinks fit, e.g. by way of a simple loan or on pro-note, or bank overdraft, or by means of a pledge or by legal or equitable mortgage or charge on any of its property, movable or immovable, including book debts, by means of debentures, debenture stock or by a floating charge on the property or whole undertaking of the Co. A Co. can also charge its uncalled capital (h). Where neither the Memo. nor articles give power to charge uncalled capital, it can be taken by a special resolution (i). Notice that a Co. cannot exercise its borrowing powers until the minimum subscription has been subscribed (see s. 149 *ante*). Different formalities have to be observed with regard to different ways of borrowing.

Formalities to be Observed for Borrowings

As regards unsecured borrowings, no special requirements are laid down except that the borrowing should be within the Co.'s statutory borrowing limits as laid down by s. 293. Where moneys are desired to be borrowed on the security of the Co.'s property, certain formalities have to be followed. Some of these are laid down by s. 125. Under the sec., every "charge" (which includes a mortgage also, under s. 124), created by a Co. on and after 1st April 1914 and being (i) a charge for the purpose of securing an issue of debentures, (ii) a charge on the uncalled capital of the Co., (iii) a charge on any immovable property of the Co. wherever situate or any interest therein, (iv) a charge on any book debts of the Co., (v) a charge on any movable property of the Co., not being a pledge, (vi) a floating charge on the undertaking or any property of the Co., including its stock in trade, (vii) a charge on unpaid calls, (viii) a charge on a ship or any share therein, and (ix) a charge on the goodwill, patent, or a licence thereunder, on a trade-mark or on a copyright or a licence thereunder, shall, so far as the security on the Co.'s property or undertaking created thereunder, be void, against the liquidator and other creditors of the Co., unless the prescribed particulars of the charge, together with the instrument (if any), creating such charge or a copy thereof, verified in the prescribed manner are filed with the Registrar for registration as required by the Act, within 21 days of the date of the creation of the charge.

The sec. further provides that the invalidity of a charge under the sec. shall not prejudice any contract or obligation to repay money secured by such charge. Further where a charge becomes void under the sec., the moneys secured thereby shall become immediately payable. Where negotiable instruments are given to a Co. by its debtors for securing book debts due to the Co., a deposit thereof to secure an advance to the Co. shall not be treated as a charge on those book debts. Secondly, holding debentures entitling the holders thereof to a charge on any immovable property of the Co. shall not be deemed to be an interest in immovable property.

The sec. further lays down that where a charge to which the sec. applies is created out of India on property outside India, the above period of 21 days shall be counted from the day on which the instrument creating or evidencing the charge could, with due diligence and in the ordinary course of post, have been received in India. Where such a charge is created in India but comprises property out of India, the instrument creating or evidencing the charge or a verified copy thereof may be filed with the Registrar within the aforesaid time, although further proceedings may be necessary to make the charge valid according to the law of such foreign country. S. 126 provides that registration of a charge as aforesaid, is notice of the charge as from the date of registration, to anyone who takes such property subsequently.

The implications and limitations of the sec. require to be carefully understood, as also the purpose for which the provisions of the sec. are framed. As s. 126 points out, the object of the above provisions is to give a fair and full notice to all persons dealing with the Co., as to how far the Co.'s property is incumbered. For this purpose, s. 125 makes certain kinds of incumbrances on the Co.'s property compulsorily registrable. These are a mortgage or charge (i) on the movable as well as immovable property (excluding, however, a pledge of the Co.'s movable property), (ii) on the uncalled capital

(h) *Re Pyle Works* (1890), 44 Ch.D. 534.

(i) *Newton v. Anglo Austria etc. Co.* (1895) A.C. 244.

or (iii) on the book debts or (iv) on unpaid calls or (v) a ship or any share therein belonging to the Co. or (vi) the goodwill, trade-mark, patent right, or copyright belonging to the Co. or on a licence given in respect of the latter two and lastly (vii) in case of a floating charge on the undertaking or property of the Co., including its stock in trade and (viii) a mortgage or charge created for securing an issue of debentures. The above kinds of incumbrances on the Co.'s properties must be registered with the Registrar as provided by the sec. It has been held in India that it makes no difference that an unregistered charge, which is void under the sec., is merged in a decree. Such a decree cannot give the creditor the position of a secured creditor in winding up (j).

Consequences of Non-registration

The consequences of non-registration should also be noted. Non-registration has the effect of making the security void, against the liquidator (if the Co. subsequently goes into liquidation) and the other creditors of the Co. This provision leads to the following results: If a mortgage or charge falling within s. 125 is not registered, it is valid as an admission of a debt but as against a creditor, e.g. a subsequent registered incumbrancer, or the liquidator, it cannot be said that a valid charge is created thereby on the Co.'s property. It has been held that a mortgage which is not registered is invalid against a subsequent incumbrancer, even if the latter had express notice of the prior mortgage at the time of taking the security. Note, however, that the security is good and valid against the Co., so long as it is a going concern, in spite of failure to register and the Co. cannot repudiate it on the ground of non-registration (k). Non-registration under the sec. does not invalidate the security (l). Further, even in cases where the security is made void by the sec., the debt or liability for which it is given is not avoided. In fact, in the words of the sec., the obligation or liability becomes immediately enforceable on the security becoming void. Further, under s. 141, the Court has power to extend the period for registration fixed by the sec. in any case where it thinks proper to do so. Further, what avoids the charge is not, it has been held, the lack of registration, but neglect to send the particulars to the Registrar as required by the sec. Where the required particulars were sent within 21 days but actual registration was not effected for 2 years, held, the charge was not affected (m).

"Book Debts" are debts arising in a business which in the ordinary course of events would be entered in the books of account of the Co. It is not necessary that they should have been actually entered in the books of account. Future "book debts" can be mortgaged or charged and a floating charge on the "book debts" of a Co. can also be created. Both must be registered under s. 125. It has been held in England that the assignment by way of security of part of the future "book debts" of a company is not a "charge" on the "book debts" of the Co., within the meaning of the sec. and therefore does not require registration (n).

Floating Charge, Its Nature

A floating charge is a charge which is ambulatory, i.e. floating with the property which it is intended to cover. It does not attach to any specific property of the Co. till the "event" on which it is to get fixed occurs. A floating charge is to be distinguished from a specific charge. In *Illingworth v. Houldsworth* (o), Lord Macnaughton distinguished the two as follows: "A specific charge, I think, is one that without more fastens on ascertained and specific property or property capable of being ascertained and defined; a floating charge, on the other hand, is ambulatory and shifting in its nature, hovering over and so to speak, floating with the property which it is intended to affect, until some event occurs or some act is done which causes it to settle and fasten on the subject of the charge within its reach and grasp." A floating charge is also to be distinguished from a future security. As Buckley L.J. pointed out in *Evans v. Rival*

(j) *Re Sathgram Coal Co. Ltd.*, 40 Cal. W.N. 1171.

(k) *Re Monolithic Building Co.* (1915), 1 Ch. 643; *Aung Ban v. Chettiar*, 5 Rang. 585.

(l) *Wright v. Horton* (1887), 17 A.C. 371.

(m) *Benares Bank v. Bank of Behar*, A.I.R. (1947) All. 117.

(n) *Ashby Warren and Co. v. Simmons*, 52 T.L.R. 613.

(o) (1904) A.C. 355.

Granite Quarries Ltd. (p), "a floating security is not a future security; it is a present security, which presently affects all the assets of the company expressed to be included in it. On the other hand, it is not a specific security, the holder cannot affirm that the assets are specifically mortgaged to him. The assets are mortgaged in such a way that the mortgagor can deal with them without the concurrence of the mortgagee. A floating security is not a specific mortgage of the assets plus a licence to the mortgagor to dispose of them in the course of his business, but a floating mortgage applying to every item comprised in the security, but not specifically affecting any item, until some event occurs or some act on the part of the mortgagee, is done, which causes it to crystallise into a fixed security". The "event" contemplated here is any of the events mentioned in the debenture on the happening whereof the moneys secured are to be immediately payable, e.g. generally, default in payment of interest for 3 months, distress or levying of execution against the property of the Co. for the period of 7 days, commencement of winding up, or the appointment of a receiver of the assets and property of the Co. It is to be noted, however, that a floating charge will not become a fixed charge till, not only any of the above events happen, but the debenture-holder takes some step thereupon, e.g. gets an appointment of a receiver to enforce the security. The charge is then said to "crystallise" or become a fixed charge. A floating charge on the undertaking or property of the Co. requires registration under s. 125.

Consequences of a Floating Charge: A floating charge enables the Co. to deal with its property in any way it is authorised to do by the Memo. or articles, so long as it remains a going concern. This has very important results. (i) The company can deal with property comprised in the charge by sale, till the charge becomes a fixed charge (q). (ii) The company, notwithstanding the floating charge, can make specific mortgages of its property having priority over the floating charge. (iii) A floating charge is also liable to be postponed to the rights of certain persons if they act before the debenture-holders take steps to enforce their security (see s. 123 *ante*). (iv) A cl. is sometimes inserted in the debentures creating a floating charge, that the Co. shall not be able to create mortgages in priority or *pari passu* with the debentures which are issued. Even in such a case a person who takes a mortgage without notice of the debenture gets priority (r). (v) Where the Co. buys land and some of the purchase money is left outstanding on a mortgage or is lent to some person who takes a charge, the charge in favour of debenture-holders is subject to the charge and mortgage so created. As to the effect of a hire purchase agreement on a floating charge, see *Re Morrison Jones and Taylor* (s).

Registration of Floating Charge: S. 125, *inter alia*, requires a floating charge on the Co.'s property or undertaking including the stock-in-trade to be registered. If not so registered, the charge is invalid against a subsequent incumbrancer as well as against the liquidator. It should be observed in this connection, however, that it does not follow that the charge will therefore be of no value at all to the Co. If it becomes a fixed charge before the Co. goes into liquidation, e.g. where the holders of the charge seize and actually take possession of the subject-matter of the charge before liquidation supervenes, the charge will be good, even against the liquidator. A floating charge on immovable properties of a Co. requires registration both under sec. 125 of the Companies Act and the Registration Act (t).

Floating Charge and Winding Up: A floating charge is valid against execution creditors till the latter take possession (u). S. 534 lays down that a floating charge on the undertaking or property of a Co. created within twelve months of the commencement of the winding up is invalid, except to the extent of the amount of any cash paid to the Co. at the time or after the creation of the charge in consideration thereof, with interest at 5 per cent, unless it is proved that the Co. immediately after the creation of the charge was solvent.

(p) (1910), 2 K.B. 979.

(q) *Law and Co. v. Pullin*, 59 Cal. 1372.

(r) *English & Scottish etc. Co. v. Brunton* (1892), 2 Q.B. 700.

(s) (1914), 1 Ch. 50.

(t) *State of Madras v. Madras Electric Co.*, A.I.R. (1956) Mad. 169.

(u) *Evans v. Rival Granite Quarries* (1910), 2 K.B. 979.

Where a Co. acquires any property, which is subject to a charge which is registrable under s. 125, the Co. shall cause the particulars of the charge, together with a copy (certified in the prescribed manner to be a correct copy) of the instrument (if any) by which the charge is created or evidenced, to be delivered to the Registrar for registration, in manner required by the Act, within 21 days after the date on which the acquisition is completed. If the property is situate and the charge is created outside India, 21 days are to be counted from the date on which a copy of the instrument could, in due course of post, if despatched with reasonable diligence, have been received in India. On default, the Co. and every officer in default are liable to a fine (s. 127).

Registration of Debentures

As noticed above, where debentures are issued containing a mortgage or charge on the Co.'s property, the same require to be registered with the Registrar. Under s. 128 where such debentures are issued in a series, containing "*pari passu*" clause (see *ante*) and accompanied by a trust deed (if any), it would be sufficient under s. 125, if within 21 days of the execution of the trust deed or execution of any debenture of the series, the following particulars are filed with the Registrar, viz. (i) the total amount secured, (ii) the date of the resolution authorising the issue of the series and the date of the covering deed, if any, (iii) a general description of the property charged, (iv) the names of the trustees of the debenture-holders (if any), together with (v) the deed of charge (if any) or a verified copy thereof, and if there is no deed, one of the debentures of the series, and (vi) where more than one issue is made, the date and amount of each issue (omission of the last does not invalidate the issue). (vii) Under s. 128, where any commission, allowance or discount is paid or agreed to be paid, directly or indirectly to any person, for subscribing or agreeing to subscribe or for procuring or agreeing to procure subscription for any such debentures, the particulars of the amount or of the rate per cent shall also be included in the particulars for registration. Failure to do so, however, does not vitiate the issue.

Where the terms or conditions of a mortgage or charge are modified, particulars thereof must also be similarly registered with the Registrar (s. 134). The Registrar is bound to keep a separate register for each company (s. 130). Where a receiver or manager is appointed by debenture-holders or in a debenture-holders' action, notice of the fact must be given to the Registrar; so also when such receiver or manager ceases to function (s. 137). Where a mortgage or charge is satisfied, that fact must also be notified to and be registered by the Registrar (ss. 138, 139). A chronological index of mortgages and charges has also to be maintained by the Registrar (s. 141). The certificate of registration when issued by the Registrar shall be *conclusive evidence* that all requirements as to registration have been satisfied (s. 132). A copy of such certificate must be endorsed on every debenture and certificate of debenture stock (s. 133).

Under s. 141, where registration of a mortgage or charge within the prescribed time has not been effected by the Co., through accident, or inadvertence or through some other sufficient cause or is not likely to prejudice the creditors or shareholders of the Co. or if it is otherwise just and equitable to grant relief in the matter, the Court can extend the time for registration, subject to such conditions as it may think fit.

Under ss. 143-144, the Co. also has to maintain a register of mortgages and charges wherein it is bound to enter *all* particulars of *all* and *every kind* of mortgage or charge created by it on its properties.

REGISTERED OFFICE

Every Co., as from the day it commences business or within 28 days of incorporation (whichever is earlier), shall have a registered office to which communications and notices to the Co. can be addressed. Notice of situation of registered office and of every change therein must be given to the Registrar within 28 days of registration or such change. The Registrar will record the same. The registered office cannot be removed, without a special resolution of the Co. (i) in case of existing Co.s outside the local limits of the city, town or village where such office is situate at the commencement of the Act or where it may be situated last by virtue of special resolution passed in that behalf; (ii)

in case of other Co.s, outside the local limits of the city, town or village where it is first situated or where it may be situated by virtue of a special resolution in that behalf. Mention of the address of the registered office in the "annual return" is not enough. In case of default, the Co. and every officer in default is liable to a fine (extending to Rs. 50 per day), the Co. so carries on business (s. 146). The Registered Office of the company is important because (i) the register of members, (ii) the register of mortgages and charges, and (iii) the minute book of general meetings are to be kept there. Inspection thereof is also to be given there. Notices, summons, and orders are also to be served there. The name of the Co., in legible letters and in characters in general use in the locality also, if the name is in different language, shall be painted or fixed and kept so painted or fixed in a conspicuous position outside every office or place where the Co.'s business is carried on. It shall also be legibly engraved on its seal, and shall also appear legibly on all its business letters, bill heads, letter papers, notices, advertisements, official publications and in all bills of exchange, hundis, pro-notes, endorsements, cheques, and orders for money or goods, signed on its behalf, and all bills for parcels, invoices, receipts and letters of credit of the Co. Where a notice, advertisement or other official publication, business letter, bill head or letter paper mentions the authorised capital of a Co., it shall also mention equally prominently, the subscribed capital and paid-up capital also. (s. 148).

Commencement of Business

Under s. 149, a Co. having a share capital which has issued a prospectus to the public, shall not commence any business or exercise its borrowing powers unless: (i) shares payable in cash, have been allotted to the extent of the "*minimum subscription*", (ii) every director has paid to the Co. for shares payable in cash, which are taken up or agreed to be taken up by him, an amount equal to the amount payable on application and allotment by the public, (iii) no money is or may become liable to be repaid to applicants for shares and debentures, by reason of failure to apply or obtain permission of a recognised Stock Exchange under s. 73 (*ante*), and (iv) unless a verified declaration by a director or secretary in the prescribed form has been filed with the Registrar stating that the above provisions have been duly complied with. A Co. with share capital, which has not issued a prospectus to the public, shall not commence any business or exercise its borrowing powers, unless: (i) a "statement in lieu of prospectus" (see *ante*), has been filed with the Registrar, (ii) every director has paid to the Co., for shares, payable in cash, taken or agreed to be taken up by him, an amount equal to the amount payable on application and allotment by the public and unless (iii) a declaration as in (iv) above is filed with the Registrar.

On the aforesaid requirements being duly fulfilled, the Registrar shall issue a *certificate to commence business*. Such certificate shall be *conclusive evidence* that the Co. is so entitled. All contracts made before the date of issue of such certificate shall be provisional only and they will be binding on the Co. on that date. The above provisions do not prevent the simultaneous offer for subscription or allotment of any shares or debentures of the Co. It does not also invalidate receipt of moneys payable on application for debentures. (The last two provisions are new.) If a Co. commences business or exercises borrowing powers in contravention of the sec., every person responsible for the same is liable to a fine. *The sec. does not apply to private companies* or to a company registered before April 1, 1914, which has not issued a prospectus to the public. The provisions of the sec., other than those relating to shares, apply to a guarantee company, which has no share capital. (This also is a new provision.)

Contracts entered into by a Co. before it is entitled to "commence business", are "*provisional*" only. "Provisional" means that the contract is to be read subject to an implied term that it shall not be binding unless and until the Co. becomes entitled to "commence business". If therefore the Co. goes into liquidation, without commencing business, such contracts cannot be enforced at all (v). The above rule is applicable to all allotments, whether first or subsequent (w).

(v) *Re Otto Electrical Co. Ltd.* (1906), 2 Ch. 390.

(w) *Mutual Bank of India v. Sobansing*, A.I.R. (1936) Lah. 790.

Register and Index of Members and Debenture-holders: Every Co. is bound to keep a register of members and enter therein: (i) the names and addresses of the members, their occupations, if any, and in the case of a Co. having a share capital, the number of shares held by each member, distinguishing each share by its number and of the amount paid or agreed to be considered as paid on the shares of each member; (ii) the date at which each person was entered in the register as member; and (iii) the date at which he ceased to be a member. Where the Co. has converted any shares into stock and given notice thereof to the Registrar, the register must show the amount of stock held by each member concerned (s. 150). Every Co. having more than 50 members must keep an index of members (card index if necessary), unless its register of members is so arranged as to constitute such index. Whenever any alteration is made in the register of members, the Co. must make the necessary alteration in the index, within 14 days. The index must contain sufficient indication to enable the account of any member in the register to be readily found out and it must be kept at the same place as the register of members. In case of default, the Co. and its officers who are knowingly or wilfully in default are liable to a fine (s. 151). Every Co. has now also to keep a register of debenture-holders in one book and enter therein (i) the name, address and occupation (if any) of each debenture-holder, (ii) the date at which each of them was entered in the register as such, (iii) the date at which he ceased to be such holder. Every Co. having more than 50 debenture-holders, must also keep an index (which may be a card index), of the names of the debenture-holders, unless its register of such holders itself constitutes such index. Every alteration in the register of debenture-holders must be entered in the Index within 14 days thereof. The index must contain sufficient indication to enable entries to be found in the register. Penalty for default is a fine for Co. and officer in default. The above provisions do not apply to debentures which on their face are payable to bearer (s. 152).

Trusts not to be entered on Register: No notice of any trust, express, implied or constructive, shall be entered on the register of members or debenture-holders, nor shall be receivable by the Registrar (s. 153). Co.s are not bound to record any kind of trust with regard to shares or debentures, so far as their registers are concerned. This however does not mean that a Co. may not be bound in certain circumstances with notice of a trust. Thus if the Co. deals with shares, on its own account, e.g. by lending money on mortgage of shares, it will be bound by constructive notice of a trust, as any other private person. The sec. also does not protect the Co., who in the face of actual notice that a shareholder is not the beneficial owner of the shares, still advances money to him on that security (x).

Closing Register: A Co. can, after 7 days' notice by advertisement in a newspaper circulating in the locality where its registered office is situate, close the register of members and that of debenture-holders for period or periods not exceeding 45 days every year, but not exceeding 30 days at one time. In case of breach of any one of the above provisions, the Co. and every officer in default is liable to a fine (s. 154).

Rectification of Register: If (a) the name of any person is, without "sufficient cause" entered in or omitted from the Register of members or (b) default is made or unnecessary delay takes place in entering on the Register the fact of any person having become or ceased to be a member, the person aggrieved, any member or the Co. can apply to the Court for rectification of the Register. The Court may reject the application or order rectification of Register. In the latter case, the Court can ask the Co. to pay damages to the aggrieved person and may make such order as to costs as it thinks fit (the provision as to damages is new).

The Court on such application may decide any question of title of any party to have his name entered or omitted from the Register, whether such question arises between members and alleged members or between such persons and the company. It may also decide any incidental questions arising with the above, if expedient or necessary.

An appeal shall lie from any order made by the Court on such application or on any issue raised on such application and tried separately. If the order is made by the District Court, the appeal shall lie to the High Court, if it is made by a single judge

of the High Court consisting of three or more Judges, it shall lie to a Bench of the Court. In case of Co.s who have to file list of members with the Registrar, the Court, in the order made under the sec., should direct the order of rectification to be filed with the Registrar within 14 days of the making thereof (s. 155).

The meaning of "*sufficient cause*" in cl. (a) has been construed in several cases. In a Bombay case (y), a shareholder had sold certain shares to another and had deposited regular transfer forms with the Co. The Co., however, went into liquidation before the transfers were approved by the Board of directors. No default or unnecessary delay was proved. *Held*, there was no sufficient cause to rectify the Register and that the shareholder's name was properly put on the Register. The effect of an order of rectification by placing the applicant's name on the Register is to restore the continuity of his membership from the time his name was illegally removed therefrom, e.g. by invalid forfeiture. He is not to be regarded as a fresh shareholder as from the date of the order (z).

Foreign Register : If authorized by articles, a Co. which has issued shares or debentures can keep in any State or country outside India a branch register of members or debenture-holders resident therein. Such register shall be called "*Foreign Register*". Within one month of the opening of such register the Co. shall file notice with the Registrar stating the place where such register is kept. On change of the place or on discontinuance of keeping such register, notice of the same should also be filed with the Registrar. Penalty for default is fine for the company and officer in default (s. 157). The foreign register shall be deemed to be part of the Co.'s principal register of members and debenture-holders. The foreign register shall be kept, shall be open for inspection and may be closed and extracts and copies therefrom may be taken in the same manner as of the principal register under the Act, except that the advertisement before closing, shall be given in a local paper circulating where such register is kept. The decision of a competent foreign Court regarding rectification of a foreign register shall be binding on the Co., if the Central Government has, by notification in the Official Gazette, notified accordingly with regard to such foreign State or country. A copy of every entry in the foreign register shall be transmitted by the Co. to the Registered Office as soon as may be. The Co. shall also keep at its registered office a duplicate of such foreign register duly posted, which shall be treated as part of the principal register. Penalty for default for the Co. and officer in default is a fine. Shares and debentures entered in the foreign register shall be kept distinct from those entered in the principal register and no transaction in regard to the former shall be entered in the principal register. A Co. may close the foreign register and thereupon all entries therein shall be transferred to other foreign registers (if any) or to the principal register. Subject to the above, a Co. may, by its articles, make rules for keeping such foreign register (s. 158).

Annual Returns

Within 42 days of holding each of its Annual General Meetings (as defined by s. 166), every company having a share capital shall file with the Registrar a return, containing the following particulars as upto that date, regarding its registered office, its register of members and debenture-holders, its shares and debentures, its indebtedness, its members and debenture-holders, both past and present, and its directors, managing directors, managing agents, secretaries and treasurers and managers past and present. The return shall be in the Form set out in Sch. V, Part II, or as near thereto as may be. The particulars (laid down by the Sch. V, Part I) are (i) address of registered office, (ii) where a foreign register is kept, name of the State or country and the address where it is kept and (iii) a *summary* distinguishing wherever possible, and giving particulars of, shares issued for cash, bonus shares and shares issued otherwise than for cash and giving following particulars with regard to each class of shares: (i) the amount of the nominal share capital of the Co. and the number of shares into which it is divided, (ii) the number of shares taken from the commencement of the Co. upto the date of the last general meeting, (iii) the amount called upon each share upto the aforesaid date, (iv) total calls received, (v) total calls unpaid, (vi) total amount (if any) paid as com-

(y) *Re Indian Specie Bank*, 40 Bom. 134.

(z) *Panna Lal v. Jagat Jit Distillery*
(1952) Pepsu 92.

mission in respect of any shares or debentures upto the said dates, (vii) discount allowed on any shares issued or so much thereof as has not been written off till the said date, (viii) total amount allowed as discount on debentures since the annual general meeting as to which the last return was submitted, (ix) total number of shares forfeited till date mentioned in (ii) above, (x) total amount of shares for which warrants are outstanding at the aforesaid date, (xi) total amount of share warrants issued and surrendered respectively since the date mentioned in (viii) above, and the number of shares comprised in each warrant, (xii) particulars of total indebtedness of the Co. upto the date mentioned in (ii) above, in respect of all mortgages and charges required to be registered with the Registrar under the Act or which would have been required to be so registered if created on and after 1st April 1914. The summary shall be accompanied by a List containing: (i) names, addresses and occupations of persons who were members on the day of the last annual general meeting, and of persons who have ceased to be members, on or before that day and since the date of the annual general meeting as to which the last return was submitted or since the incorporation of the Co., in case of a first return, (ii) stating the number of shares held by each existing member at the date of last annual general meeting and specifying shares transferred since then or since the first incorporation of the Co. by existing members or by persons who have ceased to be members, and dates of registration of the transfer (an index should be annexed if names are not arranged in alphabetical order). Where shares are converted into stock, particulars of stock held by each member should be stated, (iii) all particulars about persons who are directors, managing agent, secretaries and treasurers, manager and secretary of the company at the date of the last annual general meeting, as are required by the Act to be stated in the Register of such persons kept under the Act (s. 159).

A Co. *having no share capital*, shall within 42 days of each of its annual general meeting, file with the Registrar a return stating: (i) address of its registered office, (ii) such particulars as regards its directors, managing agent, secretaries and treasurers and manager as are required by the Act to be entered in the Register of such persons required to be kept under s. 303, (iii) particulars of the total amount of the indebtedness of the Co. upto the aforesaid date in respect of all mortgages and charges required to be registered under the Act or under any provisions of previous Companies Act or which would have been required to be registered if created after the commencement of the Acts (s. 160).

The copy of the annual return filed with the Registrar as above, shall be signed both by a director and by the managing agent, secretaries and treasurers, manager or secretary, and where these latter do not exist, by two directors, one of whom shall be the managing director. It shall be accompanied by a certificate by both the above persons stating that the return states the facts correctly and completely as required and in case of a *private Co.*, that each of the three requirements with regard to such Co.s have been duly fulfilled (s. 161). If default is made in complying with the above requirements, the Co. and every officer in default, is liable to a fine.

Inspection of Register and Index: The Register of members and Index, commencing from the date the Co. is registered, the register and index of debenture-holders, copies of annual returns, together with copies of certificates and documents annexed therewith, shall be kept at the registered office of the Co. and shall, subject to such reasonable restrictions as the Co. may impose, so that not less than 2 hours are allowed each day for inspection and subject to rules as regards closure of the registers of members and debenture-holders, be open during business hours to the inspection of any member and debenture-holder without fee, and in case of outsiders on payment of fee of Re. 1 per inspection. Any such member or debenture-holder or outsider may also make extracts therefrom without further fee. A member or debenture-holder or outsider may also require a copy of the register, index or copy or any part thereof on payment of 6 annas for every 100 words. The Co. is bound to send such copy within 10 days next after the day of the receipt of the request (exclusive of non-working days). If any inspection or copy under this sec. is refused, the Co. and every officer in default shall be liable to a fine not exceeding Rs. 50 for each offence for every day the offence continues. The Court may also order immediate inspection of the register and the index of members or may direct extract or copies thereof to be furnished immediately (s. 163). The register of members, and of debenture-holders, the annual returns, certificates and statements

referred to above shall be *prima facie* evidence of all matters directed or authorised to be entered therein (s. 164).

MEETINGS

In so far as the Co.'s administration requires the sanction of the shareholders, and in cases where the shareholders themselves desire it, the directors are empowered to call and hold meetings of shareholders. Various kinds of meetings are recognised in Company Law. A meeting may be (i) an ordinary general meeting or (ii) annual general meeting, or (iii) Statutory Meeting or (iv) an extraordinary general meeting.

Statutory Meeting: Under s. 165, every Co. limited by shares and every guarantee Co., having a share capital, is required by the Act, to hold a "Statutory Meeting", within a certain fixed period of the formation of the Co. The object of such meeting is that the shareholders shall have, at the earliest possible opportunity after the formation of the Co., a full and complete report, as to how the Co. which they helped to form, has progressed, how much of their expectations of public support has been realised and what are the future prospects of the Co., having regard to its then position, so that they may consider and decide, whether the corporate enterprise should continue any further or whether it should, in the best interests of the Co., terminate and be wound up.

The sec. provides that every Co. limited by shares, and every Co. limited by guarantee and having a share capital, shall within not less than 1 month, and not more than 6 months, from the date at which the Co. is entitled to commence business, hold a general meeting of the members of the Co. which shall be called the "*statutory meeting*". The directors shall, at least 21 days before the day on which such meeting is held, forward a report called the "*statutory report*" to every member of the Co. If the Report is forwarded later, it shall be deemed to be duly forwarded if agreed to by all the members entitled to attend and vote at the meeting. The Report shall be certified by at least two directors of the Co., one of whom shall be the managing director (if there is any), and shall be certified as correct by the auditors of the Co., so far as it relates to shares allotted, cash received with regard to such shares and receipts and payments of the Co. on capital account. The directors shall cause a copy of the report to be delivered to the Registrar for registration forthwith after copies are sent to members. A list of members of the Co. with their names and occupations, addresses and the number of shares held by each, shall be produced by the directors at the commencement of the meeting and the same shall be kept open for the inspection of members during the continuance of the meeting. The members present shall be at liberty to discuss any matter relating to (i) the formation of the Co. or (ii) arising out of the Statutory Report, whether notice thereof has been given beforehand or not, but no resolution may be passed of which notice in accordance with the Act has not been previously given. The meeting may adjourn from time to time and at such adjourned meeting, any resolution of which notice has been duly given in accordance with the Act, either before or after the first meeting, may be passed and the adjourned meeting shall have the same powers as the original meeting. Where a winding up petition is presented for failure to file the statutory report or hold the statutory meeting, the Court, instead of ordering a winding up, may direct the report to be filed or the meeting to be held or make such other order as may be just. In case of default in complying with the provisions of the sec., every director and officer in default is liable to a fine. *The sec. does not apply to private Co.s.*

The terms of a contract mentioned in a prospectus cannot be varied till the Statutory Meeting is held, except with the approval of the meeting (s. 61). The sec. does not apply to unlimited Co. or to guarantee Co., not having share capital. Notice convening the Statutory Meeting must state the meeting to be such specifically (a).

The *Statutory Report* shall state: (i) the total number of shares allotted, distinguishing those allotted as wholly or partly paid up otherwise than in cash; in case of partly paid-up shares, the extent to which they are so paid up and in either case, the consideration for which they are allotted, (ii) the total amount of cash received by the Co. in respect of all the shares allotted, distinguished in the manner aforesaid, (iii) an abstract

(a) *Gardner v. Iradale* (1912), 1 Ch. 700.

of the receipts of the Co. and of the payments made thereout upto 7 days of the date of the report, showing under distinct headings, the receipts from shares, debentures and other sources, the payments made thereout, the balance in hand, and an account or estimate of the preliminary expenses, showing separately any commission or discount paid or to be paid for issue or sale of shares or debentures; (iv) names, addresses and occupations of the directors, auditors, managing agents, secretaries and treasurers and managers (if any), and secretary of the Co. and changes, if any, which have occurred since the date of incorporation; (v) particulars of any contract which or the modification or proposed modification of which is to be submitted to the meeting for its approval, together with the particulars of the modification or proposed modification; (vi) the extent to which each underwriting contract has been carried out and reasons therefor; (vii) the arrears (if any) due on calls from directors, managing agents (where the managing agents are a firm, from any partner thereof and where they are a private Co., from every director thereof), from secretaries and treasurers (where they are a firm, from every partner thereof and where a private Co., from any director thereof) and from managers; (viii) particulars of any commission or brokerage paid or to be paid in connection with issue or sale of shares or debentures to any director, managing agent (any partner thereof, if they are a firm and any director thereof, if they are private Co.), to the secretaries and treasurers (where they are a firm, to any partner thereof and if a private Co., to every director thereof), and to the manager (s. 165).

Annual General Meeting: Under s. 166, in addition to any other meeting, every Co. shall hold an "annual general meeting". The first such meeting must be held within 18 months of the incorporation. The next such meeting must be held within 9 months of the expiry of the financial year in which the first annual general meeting was held. Succeeding annual general meetings shall also be similarly held within 9 months of the expiry of each financial year. The Registrar has power for special reasons, to extend time for such meetings for a further period of 6 months (*except in case of first annual general meeting*). Except where extension of time is granted as above, not more than 15 months should elapse between the holding of such meetings. Annual general meeting must be called on a day which is not a public holiday and during business hours. It must be held at the Registered office or some other place in the town or village where such office is situate. Notice calling the meeting shall specify such place.

If an annual general meeting is not called as above, a new power is now given to the *Central Government* to call such meeting by s. 167 under which, on the application of any member, the Central Government may call or direct the calling of such meeting and give all necessary or consequential directions in that behalf. The directions may include direction that one member present in person or by proxy shall constitute a meeting. A general meeting held under such directions shall be deemed to be the annual general meeting of the Co. If default is made in the holding of an annual general meeting, under s. 166 or in complying with the directions under s. 167, the Co. and every officer in default is liable to a fine (s. 168).

The annual general meeting is important because it is at this meeting that the annual balance sheet, profit and loss account and the auditor's report are placed before the members (s. 210). Dividends, if any, are also declared at this meeting. The shareholders are thus enabled to take a complete stock of the past year's working of the Co. and they can also get such information and elucidation in respect thereof as they may require from the directors. An extraordinary general meeting is not the same thing as an annual general meeting. A notice convening an extraordinary general meeting, therefore, cannot be construed as one for the annual general meeting (b).

Extraordinary General Meeting called on Requisition: Extraordinary General Meetings of a Co. are meetings which are called on special occasions or in emergencies. S. 169 lays down special provisions for calling such meetings on a requisition by shareholders in that behalf. Under the sec., in case of Co.s having share capital, on the requisition of shareholders holding not less than 1/10th of the paid-up capital of the Co., carrying at that date voting rights with regard to the matters in question, and in case of Co.s not having share capital, on the requisition of members holding not less than

(b) *Emp. v. Nasurbhai*, 25 Bom. L.R. 224.

1/10th of the total voting power of the Co., entitled to vote at that date on the matter in question, the Board shall forthwith duly proceed to call an extraordinary general meeting of the Co. The relevant date for the above purposes is the date of the deposit of the requisition at the registered office of the Co. The requisition must state the matters for considering which the meeting is called and must be signed by the requisitionists. It may consist of several documents, each signed by one or more of them. Where two or more matters are to be considered, the above proportion as regards shareholding and voting power shall be maintained for each matter. If within 21 days of the due deposit of a valid requisition as above, the Board does not proceed duly to call an extraordinary general meeting as required, at a date not later than 45 days from the date of deposit, such meeting may be called by the requisitionists themselves, or (in case of Co. having a share capital), by a majority of them, holding either a majority in value of paid-up capital or not less than 1/10th of the paid-up share capital (whichever is less), in respect of total shares held by the requisitionists, and in case of Co. not having a share capital, by requisitionists holding not less than 1/10th of the voting powers of the requisitionists in question. Failure on the part of directors to give notice as required by s. 189, in case of special resolution, shall be deemed to be equal to not duly convening the meeting on the part of the directors.

Requisitionists' meeting shall be called in the same manner, as far as possible, as the meetings to be called by the Board. Such meeting, however, cannot be called after 3 months of the deposit of the requisition. Of course, a meeting duly convened within 3 months, can be validly adjourned to beyond that period. Reasonable expenses incurred by the requisitionists for calling such meeting shall be paid by the Co., which can retain the same out of the fees or other remuneration payable to the directors in default. One-tenth proportion referred to in the sec. refers to that part of the issued capital on which all calls have been paid and not one-tenth of the issued capital the holders whereof have paid all calls (c).

General Meeting: The term is generally confined to the Annual General Meeting which is required to be held by the Co. at specified times. Articles however usually give power to the directors to call other general meetings. Directors must duly pass a resolution at their own duly convened meeting for calling such general meetings (d). A general meeting irregularly called, however, can be regularised by the directors duly sanctioning the same before the meeting is held (e). Directors in calling such meeting must consider the general interest of the Co. (Palmer, p. 142).

Under reg. 47, Table A, all general meetings except annual general meetings shall be called *extraordinary general meetings*. The Board, whenever it thinks fit, can call an extraordinary general meeting. If there are no sufficient directors present in India to form a quorum, any director or any two members of the Co. can call such meeting in the same manner as the Board could have called it (reg. 48).

Meeting convened by Court: Under s. 186, where for any reason it is "impracticable" to call a meeting of the Co. (other than the annual general meeting), in the manner in which they may be called, or to hold or conduct such meeting, as prescribed by the Act or the articles, the Court may, on its own motion or on the application of a director or member entitled to vote thereat, order the meeting to be called, held or conducted, in such manner as the Court may think fit. The Court can give such ancillary and consequential directions with regard to the same as it may deem expedient, modifying or supplementing the relevant provisions with regard thereto in the Act or the articles. Directions may include one that one member present in person or by proxy will constitute the meeting. Any meeting called, held or conducted as aforesaid, shall be deemed to be duly called, held and conducted.

General Provisions as regards Meetings: Ss. 170-186 lay down the provisions regarding meetings generally. As regards general meetings of public Co.s (and of private Co.s which are subsidiaries of such Co.s), these provisions are to apply, "notwithstanding anything to the contrary in the articles". As regards private Co.s (other than

(c) *Fruit etc. Ass. v. Kekwitch* (1912), 2 Ch. 52.

(d) *Re Haycroft Gold Reduction etc. Co.*

(1900), 2 Ch. 230.

(e) *Hooper v. Kerr Stuart and Co.* (1900), 83 L.T. 729.

above), these rules are to apply, "unless otherwise specified therein or unless the articles otherwise provide". As regards meetings of any class of members or debenture-holders or class of debenture-holders, the provisions of s. 176 relating to proxies, shall apply with such adaptations and modifications as may be prescribed and the provisions of ss. 171-175 (length of notice, statement and quorum) and of ss. 177-186 (rules regarding conduct of meetings), shall apply subject to such modifications and adaptations as may be prescribed, unless (i) the articles (ii) or the contracts binding the persons concerned otherwise provide (s. 170).

A general meeting can be called by 21 days' notice in writing. A shorter notice will be valid if assented to in case of annual general meeting, by all the members entitled to vote thereat, and in case of any other meeting, if assented to by holders of 95% of the paid-up share capital, entitled to vote thereat (if the Co. has share capital), and if it has no share capital, by 95% of the voting power entitled to vote thereat. Where several matters are to be considered the above proportion shall be observed in case of each matter. 21 days means 21 clear days, i.e. excluding date of notice and date of meeting (s. 171) (f).

Notice shall specify the place, the day and the hour of meeting and a statement of the business to be transacted thereat (s. 172). Where items of "special business" are to be transacted at a meeting, there shall be annexed to the notice, a statement setting out all material facts concerning each item of such business (g), and particularly the nature and extent of the interest of any director, managing agent, secretaries and treasurers, and manager (if any). Where any document has to be approved at the meeting, the time and place at which the document can be inspected shall also be stated. In case of annual general meeting, all business to be transacted thereat, except (i) consideration of the accounts and balance sheet, (ii) declaration of dividend, (iii) the appointment of directors in place of those retiring and (iv) the appointment and fixing of remuneration of auditors shall be treated as "special business". In case of other meetings, all business shall be deemed to be "special". In cases of Co.s having share capital, and Co.s whose articles provide for voting by proxy, the notice shall state, with reasonable prominence, that a member entitled to attend and vote, is entitled to appoint a proxy or one or more proxies (where allowed), to attend and vote instead of himself and that a proxy need not be a member. On default, officer in default is liable to a fine [s. 176(2)].

S. 174 provides that unless articles provide for a larger number, 5 members present in person in case of public Co. and 2 members present in person in case of a private Co. shall constitute *quorum* for Co. meetings [see reg. 49(2), Table A]. It is clear, therefore, that except where so ordered by the Court (under s. 186) one member cannot form a meeting by holding proxies from others (h). Number of members to form a *quorum* is generally fixed by the articles.

Each shareholder has one *vote* ordinarily, either on a show of hands or on poll [see new s. 87(1)]. The articles usually provide, however, that the voting power shall depend on the number of shares held by each member. Only the person whose name appears on the register as member can vote. It has been held recently that a person whose name appears on the register as a member may be required by the Court to vote in a certain manner, according to the wishes of another person, who, though not a member, has a better title to the shares, e.g. a mortgagee of shares (i). Voting generally takes place in the following manner. The chairman first takes a show of hands. In this, each member present counts as one vote, though the member may hold a number of proxies for others. Before or on the declaration of the result of the show of hands by the chairman, a poll may be demanded. On poll, voting rights of members shall be as laid down in s. 87 (see *ante*). In case of joint-holders, the right to vote in person or by proxy shall ordinarily vest in the person whose name stands first on the register (see reg. 57, Table A). A lunatic so found by Court may vote by his committee or other legal guardian and the latter can, on poll, vote in person or by proxy (reg. 58, Table A).

(f) *Rex v. Turner*.

(g) *Pacific Coast Coal Mines v. Arbuthnot*
(1917) A.C. 607.

(h) *Re Prain and Sons Ltd.* (1947) Sc.L.T.
289.

(i) *Puddphatt v. Leith* (1916) 1 Ch. 200.

Articles may provide that no member shall be entitled to vote unless all calls or other sums presently payable by him in respect of shares held by him have been paid. Such provision is valid (s. 181) (see reg. 59, Table A). Any prohibition or restriction on a member's right to vote at a meeting, except as provided by s. 181 and in particular that he should hold the shares for a particular period before the meeting, shall be void in case of public companies and private companies which are subsidiary of such companies.

At any general meeting, a resolution put to vote, shall be decided on a *show of hands*, unless a poll is demanded as laid down by s. 178 (s. 177). A declaration by the chairman on a show of hands that a resolution has or has not been carried, or has or has not been carried either unanimously or by a particular majority, together with an entry to that effect in the minute books of the Co. shall be conclusive evidence of the aforesaid facts, without proof of the number or proportion of votes cast for or against the resolution (s. 178).

S. 176 provides that every member entitled to attend and vote shall be entitled to appoint a *proxy* to attend and vote for him at the meeting. The proxy may or may not be a member. A proxy so appointed shall not have the right to speak at the meeting.

Unless the articles otherwise provide, the above provisions are not to apply to Co.s not having share capital. Further, unless the articles otherwise provide a member of a private Co. shall not be entitled to appoint more than one proxy to attend on the same occasion. Lastly, unless the articles otherwise provide, a proxy shall not be entitled to vote, except on a poll. Every notice calling a meeting shall state that a member is entitled to appoint one or more proxies as the case may be. Penalty for default is a fine for every officer in default.

In case of public Co.s and private Co.s which are subsidiaries of such Co.s, articles requiring a proxy or instrument showing the validity of a proxy to be deposited with the Co. or any other person, more than 48 hours before such meeting, shall be void.

No invitation to appoint as proxy, a person or persons mentioned therein shall be sent out at the Co.'s expense to any member entitled to notice of meeting and to vote thereat by proxy. Every officer who knowingly issues or wilfully authorises or permits such issue, is liable to a fine. No punishment however is incurred by issuing, at a members' written request, a form of appointment, naming the proxy or a list of persons willing to act as proxies, provided such form or list is available to all members.

The instrument appointing a proxy shall be in writing and signed by the appointer or by his attorney duly authorised in writing. If the appointer is a corporate body, it must be under its seal, or be signed by an officer or attorney duly authorised. A proxy, if in any of the forms set out in Sch. IX, shall not be questioned on the ground that it does not comply with any special requirements of the articles. Every member entitled to vote at a meeting, or on any resolution to be moved thereat, shall be entitled to inspection of proxies, during 24 hours before the time fixed for the meeting and till the conclusion of the meeting, at any time, during business hours of the Co., provided not less than 3 days' notice in writing in that behalf has been given by him to the Co.

Before or at the time of declaration of result on show of hands, a poll may be ordered to be taken by the chairman on his own motion. The chairman shall be bound to order a poll to be taken if demanded (i) in case of public Co. by at least 5 persons entitled to vote on the resolution, present in person or by proxy; (ii) in case of private Co. by one member entitled to vote on the resolution, present in person or by proxy, if not more than 7 such persons are personally present, and by two such members present in person or by proxy, if more than 7 such members are personally present; (iii) by any member or members present in person or by proxy, having not less than 1/10th of the voting power regarding the particular resolution, and (iv) by any member or members present in person or by proxy, holding shares (conferring a voting right on the resolution) on which the paid-up amount is not less than 1/10th of the total amount paid up on all the shares of that class. Demand for a poll may be withdrawn at any time by persons who made it (s. 179). A poll on adjournment shall be taken forthwith, on any other question (except election of chairman under s. 174), it shall be taken within 48 hours of the demand, as the chairman may direct (s. 180). On a poll, a

member entitled to more than one vote or his proxy or other person entitled to vote for him, shall not be bound to cast all his votes or cast in the same way all the votes he has (s. 183). Where poll is to be taken, the chairman shall appoint two *scrutineers* to scrutinise the votes and report the result to him. Before the declaration of the result, the chairman shall have power to remove a scrutineer and appoint another in his place. One of the scrutineers shall always be a member present at the meeting (if willing) and not being an officer or employee of the Co. (s. 184). The chairman shall have power to regulate the manner of taking the poll, subject to the provisions of the Act. The result of the poll shall be deemed to be the decision of the meeting on the resolution on which poll was taken (s. 185).

RESOLUTIONS

Circulation of Members' Resolution: S. 188 provides a method by which members desirous of moving a resolution at the annual general meeting can give notice and explanation in advance to the other members of what they intend to do. Under the sec., on the written requisition of not less than 1/20th of the total voting power of all members entitled to vote on the resolution at that date, or on a requisition of 100 members, holding shares on which Rs. 1 lakh in all has been paid up, the Co. shall be bound, at the expense of the requisitionists (unless the Co. otherwise decides), to serve notice of any proper resolution intended to be moved by the requisitionists at the annual general meeting on all members entitled to receive notice of such meeting, and also a statement (of not more than 1,000 words) with regard to the said resolution or the business to be transacted at the meeting. Notice shall be served on members entitled to attend the annual general meeting in the same manner as notice of annual general meeting by serving copy of resolution or statement and on other members by serving on them the general effect of the resolution in same manner as notice of general meetings are served. Service shall be effected the same time the notice of meeting is served on members or as soon thereafter as practicable. Accidental omission to serve will not invalidate circulation. Requisition for circulating resolution must be deposited at the registered office 6 weeks, and any other requisition 2 weeks, before the meeting, together with reasonable expenses of circulation. If the annual general meeting is called within less than 6 weeks of the deposit, however, such deposit shall be regarded as proper. The Co. shall not be bound to circulate a resolution or statement if the Court finds, on application by the Co. or an aggrieved person, the same to be defamatory or abuse of the provisions of the sec. Costs of such application may be thrown on the requisitionists though no party to the application. The Co. shall be bound to include a resolution circulated as above in the business of the annual general meeting, any accidental omission in service being immaterial. Penalty for default is a fine for every officer in default.

Three kinds of resolutions are recognised by the Act: (i) ordinary, (ii) special, and (iii) resolution requiring special notice. An *ordinary resolution* is one which is passed at a general meeting, of which due notice as required by the Act has been given (see ante) by a simple majority of members entitled to vote thereon [s. 189(i)], [i.e. where votes given (in person or by proxy if allowed) including the chairman's casting vote (if any) exceed votes cast against the resolution].

Special Resolution: A resolution shall be "*special*" when: (i) the intention to propose the resolution as special resolution has been duly specified in the notice or other intimation convening the general meeting; (ii) notice required under the Act for such resolution has been duly given; and (iii) the votes cast in favour of the resolution (on show of hands in person and by proxy on poll) are not less than 3 times the number of votes cast against it by members entitled to vote thereon [s. 189(2)].

A "*special resolution*" is one of the most important instruments by which incorporated Co.s carry out important executive or administrative acts which are or may be necessary for the Co.'s benefit. Such a resolution is now required for: (i) alteration of place of registered office of Co. from one State to another and for alteration of its objects (s. 17), (ii) for changing its name (s. 21), (iii) for alteration of articles (s. 31), (iv) for creating reserve capital (s. 99), (v) for reduction of capital (s. 100), (vi) for removing registered office from where it is, to another place in the same State (s. 146), (vii) for paying interest out of capital (s. 208), (viii) for appointment of inspectors to

investigate (s. 237), (ix) for sanctioning appointment of persons closely connected with managing agents as directors (s. 261), (x) for fixing remuneration of directors if the articles require such resolution (s. 309), (xi) to sanction remuneration to a director on percentage of profits basis in certain cases (s. 309), (xii) for sanctioning the holding of office or place of profit under the Co. by director, managing agent, secretaries and treasurers and others (s. 314), (xiii) for making the liability of any director, managing agent, secretaries and treasurers or manager unlimited (s. 323), (xiv) for removing managing agent for gross negligence or mismanagement (s. 338), (xv) for sanctioning additional remuneration beyond 10 per cent to managing agent (s. 352), (xvi) for appointing managing agent and his associate as selling agents of Co. outside India (s. 356), (xvii) for permitting managing agent and his associate to procure business of supply and rendering services to the Co. from outside India (s. 357), (xviii) for appointing managing agent and his associate as Co.'s buying agents outside India (s. 358), (xix) for permitting managing agent and his associate to sell, purchase, or supply any property or services to or from the Co. and for underwriting shares or debentures of the Co. (s. 360), (xx) for sanctioning loans or guarantee or security to Co.s under the same management (s. 370), (xxi) for permitting managing agent or his associate to carrying on competing business (s. 375), (xxii) for voluntary winding up the Co. (s. 484), and (xxiii) for disposing of books and papers in voluntary winding up after the same is completed (s. 550).

“Special Notice” Resolutions : A third class of resolutions are those which by the Act or articles require a “*special notice*” to be given in respect of them (s. 190). Special notice resolutions are required: (i) for the appointment of an auditor other than the retiring auditor (s. 225), (ii) for resolution that retiring auditor shall not be re-appointed (s. 225), (iii) for appointing as directors certain persons who are closely connected with managing agent, etc. (s. 261), (iv) for the appointment of a director who is overage (s. 281), (v) for removing a director before his term expires (s. 284), and (vi) for appointing another person as director in place of the director removed (s. 284).

The “*special notice*” above referred to is to be given as follows: notice of intention to move the resolution shall be given to the Co. 28 days before the meeting, the day of service of notice and the day of meeting being excluded. The Co. shall give notice of the resolution along with notice of the meeting; if that is not practicable, by advertisement in a local newspaper or any other mode allowed by the articles 21 days before the meeting. If after notice of the resolution is duly given to the Co., a meeting is called less than 28 days thereafter, the notice, though not in time, shall be deemed to be proper (s. 190).

Resolutions passed at an adjourned meeting of the Co. or of a class of shareholders or of the Board, shall be deemed to have been passed at the date on which in fact they are passed, and not at any earlier date (s. 191). This is important in that it fixes the date when resolutions passed at an adjourned meeting are to be deemed to have been passed. They are deemed to have been passed on the date of the adjourned meeting at which they are in fact passed, and not on the date of the original meeting.

Registration of Special Resolutions and Agreements

Certain resolutions and agreements made by a Co. have to be filed with the Registrar under s. 192. These are: (i) special resolution, (ii) resolutions which have been agreed to by all the members of a company, but which, if not so agreed to, would not have been effective for their purpose unless they had been passed as special resolutions, (iii) resolutions of the Board or agreements executed by the Co., regarding appointment, reappointment, renewal of appointment or variation of terms of appointment, of a managing director, (iv) agreements relating to the appointment, reappointment, or renewal of appointment of managing agent or secretaries and treasurers or varying the terms thereof, executed by the Co., (v) resolutions or agreements which have been agreed to by all members of a class of shareholders, but which would not have been effective unless passed by a particular majority or in a special manner and all resolutions and agreements which are binding on all members of a class, though not agreed to by all of them, and (vi) resolutions for voluntary winding up under s. 484(i). Printed or typed copies of the above resolutions and agreements, duly certified by an officer of the Co., must

be filed with the Registrar within 15 days of the passing or making thereof, who will record the same. Penalty for default is a fine for the Co. and the officer in default. Every copy of articles issued subsequently shall have embodied therein or annexed thereto copies of such resolutions and agreements. Where articles are not registered, a printed copy of the above shall be forwarded to any member at his request (fee Re. 1). Penalty for default is a fine for the Co. and the officer in default. "Officer" in both the above cases includes a liquidator.

Minutes of Board Meetings and General Meetings

S. 193 provides that every Co. shall cause minutes of general meetings and Board meetings and of meetings of Board Committees, to be entered in books kept for that purpose. The minutes shall contain a fair and correct summary of the proceedings of every such meeting. Appointments of officers, if made at such meetings, shall be included in the minutes. In case of Board meetings, the minutes shall also contain (i) names of directors present, (ii) names of directors dissenting or not concurring with any resolution passed thereat. Defamatory matters, irrelevant or immaterial matters and matters detrimental to the interests of the Co. shall not be entered in the minutes. The Chairman shall have absolute discretion as to which matters should be disallowed on the above grounds. Penalty for default is a fine for Co. and officers in default. Such minutes signed by the Chairman of the meeting or of the next succeeding meeting shall be evidence of the proceedings at the meeting (s. 194). On such minutes being signed as aforesaid, a presumption will arise that the meeting was duly called and held, that all proceedings thereat have duly taken place and that all appointments of directors and liquidators made thereat, were valid (s. 195). Under s. 197, no report of proceedings at general meeting shall be circulated or advertised at the expense of the Co., unless matters required to be included in the minutes under s. 192 above are included therein. Penalty for default is a fine for each offence for Co. and officer in default.

The Minute Book of the general meetings of the Co. held after 15th January 1937, must be kept at the registered office of the Co. and must be kept open for inspection of members without fee during business hours subject to such reasonable restrictions, as the articles or the Co. in general meeting may place, but so that not less than 2 hours are allowed each day for inspection. Copies of minutes must be furnished to members within 7 days of demand. Failure to give inspection or furnish copies as above entails penalty for Co. and officer in default. The Court may also order immediate inspection and copies (s. 196).

Irregularities

Where a Co., in the matter of its internal management, acts irregularly or not in complete accordance with its articles, the general rule followed, in granting relief to those who complain of the irregularity, is that the Court will not interfere at the instance of minority to correct irregularities, the acts themselves being not *ultra vires*. This is known as the *Rule in Foss v. Harbottle* (j). In this case a suit was brought by two shareholders against the directors and others, alleging that the directors had bought at an excessive price certain lands from themselves for the payment of which they had now mortgaged the Co.'s property in a manner not authorised by the articles. The suit however was dismissed on the ground that injury, if any, was an injury to the corporation as a whole, inflicted on it as a "*cestui que trust*" by its trustees, and it was, therefore, for the corporation to deal with it. The principle underlying the above rule was thus stated by Mellish L.J. in *Macdoughall v. Gardner* (k): "if the thing complained of is a thing which in substance the majority of the company are entitled to do regularly or if something has been done illegally which the majority is entitled to do legally, there is no use in having litigation about it, the ultimate end of which is only that a meeting has to be called and then ultimately the majority gets its wishes". In other words, where there is no infringement of the individual right of a shareholder but a possible injury to the Co. as a corporate body, the Co. alone can sue, the principle being that since it would be with the Co. to ratify, it must also be with the Co. to challenge the acts complained of by suit or otherwise. In such cases, a suit by one

(j) 2 Hare 461.

(k) (1875) 1 Ch.D. 13.

or more shareholders will be incompetent, but the Co., as such, must file the suit, if at all. Thus irregularities committed in convening a meeting and in the conduct of the meeting at which some resolutions are passed, will not be interfered with by the Court at the instance of a minority, even though suing on behalf of themselves and all the other shareholders except the defendants (i.e. the majority) (l).

The stringency of the above rule however has been relaxed in modern times as Swinfen Eady J. pointed out in *Baillie v. Automatic Telephone Co. (m)*, and where justice requires it, e.g. where shareholders who have no remedy otherwise, would be debarred from taking steps to ventilate their grievances in a Court of Law, a suit by the minority against the Co. will be allowed. As the Bombay High Court said in *Parshram v. Tata Industrial Bank (n)*, "irregularities in the proceedings at the meeting of the company are not matters for Court. The court will only interfere (i) if the rights of the shareholders are injured (ii) in case of fraud or (iii) if ultra vires action is made out."

ACCOUNTS AND AUDIT

Books of Account of Company: S. 209 provides that every Co. shall keep at its registered office or any other place in India as its directors think proper, proper books of account with respect to: (i) all sums of money received and expended by the Co. and the matters in respect to which the receipts and expenditure took place, (ii) all sales and purchases of goods by the Co. and (iii) the assets and liabilities of the Co. With regard to branch offices, it is sufficient if proper books of account showing transactions of such offices are kept thereat and proper summarised returns made up every three months are sent by such offices to the Registered office or the other place mentioned above. Books will not be deemed to be properly kept if they do not give a "fair and true" view of the state of affairs of the Co. or its branch or do not explain the transactions. The books shall be open to inspection of directors, during business hours. The responsibility for keeping such proper books shall be on managing agent or secretaries and treasurers (if any); if any of these persons are a firm, on every partner thereof and if an incorporated body, on every director thereof. If the Co. has no managing agent, or secretaries and treasurers, the responsibility shall be on every director of the Co. If any of the above persons fails to take reasonable steps to secure compliance by the Co. with the requirements of the sec. or has become by his wilful act the cause of such default, the penalty is a fine. If prosecuted under the sec., however, it will be good defence to show that the party had reasonable grounds to believe and did believe that a competent and reliable person was charged with the above duties and was in a position to discharge the same. In such cases, the person in charge is liable to a fine for each default.

Annual Accounts and Balance Sheet: S. 210 provides that the Board shall, at every annual general meeting, lay before the Co. the "balance sheet" and a "profit and loss account" of the Co. made up as stated below: Where the Co. is not carrying on any business for profit, an "income and expenditure account" shall be laid before the annual general meeting in place of "profit and loss account". References to "profit and loss account" in the sec. shall, with regard to such Co., be treated as reference to "income and expenditure account".

In case of the first annual general meeting, the "balance sheet" and "profit and loss account" shall relate and extend to the period from the date of incorporation upto 9 months before the date of the meeting; in case of subsequent annual general meetings, from the date immediately after the period for which the account was last submitted, upto 9 months before the date of the meeting and if extension of time is granted under s. 166(1) (a), upto 9 months and the extension granted, before the date of the meeting. The aforesaid period is called the "financial year". It may be more or less than a calendar year but shall not exceed 15 months. It may be extended to 18 months, if the Registrar grants special permission in that behalf. Any director failing to take reasonable steps to secure compliance with the above requirements, is punishable with imprisonment or fine or both, for each offence. S. 211 provides that the "balance sheet" and

(l) *Cotton v. National Union of Seamen* (1929) 2 Ch. 58.

(m) (1915) 1 Ch. 503.

(n) 25 Bom. L.R. 1083.

"profit and loss account" shall respectively give a "fair and true" view of state of affairs of the Co., as at the end of and for the financial year and shall be in forms set out in Parts I and II respectively, of Schedule VI, so far as circumstances admit and the said forms are applicable. The above does not apply to insurance and banking companies and to other companies which have been provided with particular forms under their governing Acts. The Central Government has power to grant exemption to any class of Co.s from compliance with the above requirements, either conditionally or otherwise, if necessary in the national interest. The Central Government has also, on the application of or with the consent of the directors, power to modify any of the above requirements, re: "balance sheet" and "profit and loss account", with regard to any Co. for adapting them to the Co.'s circumstances.

An Insurance Co., a Banking Co., and an Electric Co. governed by the Electric Supply Act, 1948, need not disclose matters not required to be disclosed respectively by the Insurance Act of 1938, by the Banking Act of 1949 and the Electricity Supply Act of 1948. A Co. need not also disclose matters which are not required to be disclosed by Schedule VI or by virtue of a notification or order of the Central Government under their aforesaid powers.

The "balance sheet" and "profit and loss account" shall be authenticated by the signature on behalf of the Board, in case of Banking companies by persons mentioned in s. 29(2), cls. (a) and (b), of the Banking Companies Act of 1949, and in case of other Co.s, by the managing agent, secretaries and treasurers, manager or secretary (if any), and by not less than 2 directors, one of whom shall be the managing director (if any). In the last case, if there is only one director in India, the above documents shall be signed by him, with a note explaining reasons for non-compliance with the sec. Both the documents shall be approved by the Board, before they are signed as aforesaid and before they are submitted to the auditors for report (s. 215). The "profit and loss account" shall be annexed to the "balance sheet" with the auditor's report attached thereto (s. 216); the Board of Directors' report shall also be annexed to the balance sheet (s. 217).

In case of public companies, three copies of the "Balance Sheet" and "Profit and Loss Account" as aforesaid, together with three copies of all documents required to be annexed thereto, shall, after they have been laid before the annual general meeting, be filed, with Registrar at the same time that the Annual Return (under s. 161) is filed with him (s. 220). The copies of "balance sheet" and "profit and loss account" shall be signed by the managing director, managing agent, secretaries and treasurers, manager or secretary of the Co. and if there be none of these, by a director of the Co. In case of a private Co., three copies of the "Balance Sheet" certified to be true by the Co.'s auditors, with the auditor's report, so far as it relates to the "balance sheet", shall be similarly filed. If the balance sheet is not adopted at the annual general meeting before which it is laid, the fact and reasons therefor, in case of both the above kinds of Co.s, shall be annexed to the balance sheet and the copies thereof filed with the Registrar. On default, penalty is the same as under s. 162 (annual return) for the Co. and officers in default.

The contents of "balance sheet" and of "profit and loss account" are subjects of Sch. VI of the Act. The Sch. contains elaborate details of items to be included. These must be studied by themselves by those concerned with preparation of balance sheets, etc.

Where a Co. is a holding Co. having subsidiaries at the end of the financial year as at which the balance sheet of the holding Co. is made out, the latter Co.'s balance sheet shall have attached thereto: (i) a copy of the balance sheet of each subsidiary which shall be in accordance with the provisions of the Act and shall be made out as at the end of its financial year next before the day at which the holding Co.'s balance sheet is made out; (ii) a copy of the "profit and loss account" of the same, and (iii) a copy of the report of the directors, and (iv) of the auditor, of the subsidiary. The "profit and loss account" and the above reports shall be in accordance with the Act and for the financial year mentioned as above (s. 212).

Directors' Report: Every balance sheet laid before the Co.'s general meeting shall have attached thereto a Report of the Board of Directors, with respect to: (i) the state

of affairs of the Co., (ii) the amounts proposed to be carried to any reserve either in the same or subsequent balance sheet, and (iii) the dividend recommended. The Report shall also, so far as material for the above purposes and if not harmful to the Co.'s or its subsidiary's interest, state the changes in the financial year (i) in the nature of the Co.'s business, (ii) in the Co.'s subsidiaries and the nature of their business, and (iii) generally in the classes of business in which the Co. has interest. Fulllest information and explanations must be given by the Board in their report or in an addendum thereto with regard to every reservation, qualification or adverse remarks contained in the auditor's report. The Chairman of the Board can sign such Report only if specially authorised in that behalf by the Board. Where he is not authorised, the report, etc. shall be signed by such number of directors as are required to sign the balance sheet and profit and loss account under s. 215(1) and (2). Every director failing to take reasonable steps to comply with the provisions of the sec. and any Chairman violating its provisions are liable for each offence to a penalty of imprisonment or fine or both, the first being permissible only if the offence is wilful. That the person prosecuted under the sec. had reasonable ground to believe and did believe that a competent and reliable person was charged with the above duty and was in a position to discharge the same would be a good defence, against a prosecution under the sec., but in such a case, the person in charge shall be liable to imprisonment or fine or both for each default, imprisonment being given only if the default is wilful (s. 217).

Auditors

S. 224 provides that auditors shall be appointed at the annual general meeting and shall hold office from the conclusion of the said meeting till the conclusion of the next. Generally the retiring auditor shall be reappointed unless: (i) he is not qualified for reappointment; (ii) he has given written notice to the Co. refusing reappointment; (iii) a resolution (as hereinafter stated) is passed at the meeting appointing another person as auditor or declaring that he shall not be reappointed; (iv) notice has been given to the Co. of a resolution to appoint another in place of the retiring auditor and the resolution cannot be moved by reason of the death, incapacity or disqualification of the person. Where no auditor is appointed at the annual general meeting, notice thereof shall be given to the Central Government within 7 days thereof and the Central Government may thereupon fill the vacancy. Failure to give notice is punishable by a fine for the Co. and officer in default. First auditors shall be appointed by the Board within one month of the registration of the Co. and they shall hold office till the conclusion of the first general meeting. If the Board fails to make such appointment, the Co. in general meeting may appoint the first auditors. The Co. in general meeting may remove such auditors and appoint other auditors nominated by any member, provided notice of such nomination has been given to the members 14 days before the meeting.

Except as regards the first auditors, an auditor appointed by the Co. can be removed only by the Co. in general meeting, after obtaining previous approval of the Central Government [s. 224(7)]. S. 225 provides that special notice (as laid down in s. 190) shall be required for a resolution at the annual general meeting for appointing another person as auditor in place of retiring auditor and for not reappointing the latter. Copy of such resolution shall be forthwith sent by the Co. to the retiring auditor. The retiring auditor shall be entitled to make written representations to the Co. in the above behalf. On his request, the Co. shall notify the members of the fact of such representations in any notice of the resolution and send a copy thereof to the members therewith, unless the representations have been received too late, in which case the auditor may require the representations to be read at the meeting. He may be heard orally also. The representations need not be notified or read, if on the application of the Co. or any aggrieved person, the Court is satisfied that they are defamatory and an abuse of the power given. Costs of the application may be ordered to be paid by the auditor in question, though no party to it. The right to receive notice as above and to make representations as above shall be enjoyed by the first auditors and other auditors sought to be removed by the Co. under s. 225.

The remuneration of an auditor appointed by the Board and the Central Government shall be fixed by them respectively; in other cases, by the Co. in general meeting or in such manner as may be determined at such meeting. Auditors' expenses are to

be included in the remuneration (s. 224). Chartered Accountants qualified under the Chartered Accountants Act of 1949 alone shall be appointed as auditors of a Co. If all members of a firm are qualified as above the firm may be appointed auditors. In Part B States, a holder of a certificate of auditor under any law of such State before Part B States Laws Act of 1951 was passed, shall be entitled to be appointed as auditor of Co.s in that State. The Central Government may make rules for such auditors (s. 226).

The following persons cannot be appointed auditors: (i) a body corporate, (ii) an "officer" or employee of the Co., or (iii) any partner or employee of the last named persons, (iv) a person indebted to the Co. for over Rs. 1,000 or who has given guarantee or security for such debtor, (v) a director or member of a private Co. or a partner of a firm, acting as managing agent, secretaries and treasurers of the Co., and (vi) a director or holder of more than 5% of the nominal capital of a corporate body which is acting as managing agent or secretaries and treasurers of the Co. This does not apply where such shares are held as trustee for another. "Officer" in the above context does not include an auditor. A person disqualified as above for a subsidiary shall be also disqualified for the holding Co. If during term of his office an auditor becomes disqualified as above, he shall be deemed to have vacated his office.

Auditors' Report: S. 227 provides that every auditor shall have a right of access at all times to all the account books and vouchers of the Co. and shall also be entitled to require from its officers such information and explanations as he thinks necessary for the performance of his duties. He shall make a Report to members on the accounts examined by him and on every balance sheet and profit and loss account and documents annexed therewith which are laid before the Co. in the annual general meetings held during his tenure of office. The Report shall state: (i) whether in his opinion and to the best of information and explanations given to him, the said accounts give the information required by the Act and in the manner required by the Act and (ii) whether the said accounts give a *true and fair view*, in case of the balance sheet, of the Co.'s affairs at the end of the financial year and in case of the "profit and loss account", of the profit and loss for the financial year. The Report shall also state (iii) whether he has obtained all the information and explanations which to the best of his knowledge and belief, were necessary for the audit; (iv) whether in his opinion proper books of account have been kept by the Co. as required by law, as appears from his examination thereof and whether proper and adequate returns have been received from branch offices and (v) whether the Co.'s balance sheet and "profit and loss account" are in agreement with the account books and the returns; (vi) where any of the above items are answered in the negative or with qualifications, the Report must state the reasons therefor; (vii) where under the provisions of the Act or any other law, a Co. is not required to disclose certain matters, and the said provisions are specified in the balance sheet and "profit and loss account", the auditor shall give the above certificates, if satisfied, that, subject to these provisions, the balance sheet and profit and loss account show the correct position of the Co.'s affairs as required by law. Accounts of a *Branch Office* shall be audited by a qualified auditor (s. 228) unless the Co. in general meeting otherwise decides. The Report and all other documents required to be signed or authenticated by the auditor, shall be signed or authenticated by the auditor of the Co. and in case of firms, by the partner practising in India (s. 229). The Report shall be read at the annual general meeting and shall be open to inspection of all members of the Co. (s. 230). All notices of and other communications relating to general meetings which a member is entitled to receive shall be forwarded to the Co.'s auditor. He shall be entitled to attend general meetings and to speak thereat on matters concerning him as auditor (s. 231). Penalty for the Co. making default with regard to provisions in ss. 224-231 is a fine for the Co. and every officer in default (s. 232). Penalty for *wilful default* on the part of the auditor in complying with the provisions of ss. 227 and 229 is a fine for the auditor and the person who wrongfully signs a report or signs or authenticates a document (s. 232).

Duties of Auditor

The duties of an auditor generally may be said to be (i) to make himself acquainted with his duties under the articles and under the Act; he is not bound to be a legal expert, however (o); (ii) to see that the books of account and the balance sheet show

the true financial position of the Co. and (iii) to report all material points to the shareholders. As Lindley L.J. said in *In re London and General Bank* (2) (p), "it is no part of an auditor's duty to give advice, either to directors or shareholders, as to what they ought to do. An auditor has nothing to do with the prudence or imprudence of making loans with or without security. It is nothing to him whether the business of the company is being conducted prudently or imprudently, profitably or unprofitably. It is nothing to him whether dividends are properly or improperly declared, provided he discharges his own duties to the shareholders. His duty is to ascertain and state the true financial position of the company at the time of the audit and his duty is confined to that. But then comes the question "How is he to ascertain that position"? The answer is "by examining the books of the company". But he does not discharge his duty by doing this, without inquiry and without taking any trouble to see that the books themselves show the company's true position. He must take reasonable care to ascertain that they do so. Unless he does this, his audit would be worse than a farce. Assuming that the books are so kept as to show the true position of a company, the auditor has to frame a balance sheet showing that position according to the books and to certify that the balance sheet presented is correct in that sense. But his first duty is to examine the books, not merely for the purpose of ascertaining what they do show but also for the purpose of satisfying himself that they show the financial position of the company". An auditor is bound to look into the accounts of the Co. and to report to shareholders what the true condition of its affairs is and whether that condition is reflected in the accounts published. He is not justified in merely accepting whatever the directors say as final (q).

Auditors are not "officers" of the Co. except for the purposes of ss. 477, 478, 539, 543, 545, 621, 625 and 633 [see s. 2(1)(30)]. There are, however, penalties laid down by the Act for auditors who fail to discharge their duties properly. (i) Under s. 233, if an auditor's report does not comply with the requirements of ss. 227 and 229, every auditor who is knowingly and wilfully a party thereto, is liable to a fine not exceeding Rs. 1,000. (ii) An auditor can also be proceeded against on a misfeasance summons under s. 543.

INVESTIGATION OF COMPANY'S AFFAIRS

Registrar's Power to call for Information: Under s. 234, where the Registrar, on the perusal of any document required to be submitted to him by the Co. under the Act, is of opinion that any information or explanation is necessary in order that such document may afford full particulars of the matters to which it purports to relate, he may, by a written order, call on the Co. to furnish in writing, such information or explanation, within such time as he may think proper. The Co. and all persons who are or have been its officers shall be thereupon bound to furnish such information or explanation to the best of their power. Penalty for default is a fine to Co., and officer in default. The Court may also, on the application of the Registrar, after notice to the Co., make an order on the Co. for the production and inspection of any documents which are reasonably required for such investigation.

Investigation of Company's Affairs: S. 235 provides that the Central Government may appoint one or more competent inspectors to investigate the affairs of any Co. and to report thereon in such manner as the Central Government may direct, (a) in case of any Co. having share capital, on the application of not less than 200 members or 1/10th of the holders of its issued share capital, (b) in the case of a Co. not having a share capital, on the application of not less than 1/5th of its registered members, and (c) in case of any Co., on the report of the Registrar under s. 234. The application by members of a Co. shall be supported by such evidence as the Central Government may require for showing that the applicants have good reasons for requiring the investigation. The Central Government may, if necessary, require applicants to furnish security for the costs of the investigation, not exceeding Rs. 1,000.

A further new power is now given to the Central Government under s. 237, to order investigation by competent *Inspectors* of the affairs of a Co. and to report to the Central

(p) (1895) 2 Ch. 673, 682.

(q) *Ganeshan v. Joscelyne*, A.I.R. (1957) Cal. 35.

Government thereon. The Central Government is bound to exercise this power if: (i) the Co. by special resolution or (ii) if the Court by order, declares that the affairs of the Co. ought to be investigated by inspector appointed by Central Government. The Central Government may exercise the power, if in its opinion there are circumstances suggestive: (i) that Co.'s business was being conducted with a view to defraud the creditors or any other persons or otherwise for a fraudulent or unlawful purpose, or in a manner oppressive to any of its members or that the Co. was formed for a fraudulent or unlawful purpose; (ii) that the persons concerned with the formation or management of the Co. have been guilty of fraud, misfeasance or other misconduct towards the Co. or to any members, (iii) that members have not been given all information about the Co.'s affairs which they might reasonably expect, including information regarding calculation of commission payable to a managing or other director, managing agent, secretaries and treasurers or manager of the Co. In no investigation as above, shall a body corporate, or an association, be appointed inspector (s. 238).

Powers of Inspector: The Inspector appointed under ss. 235 and 237 shall have power, if necessary for his investigation, to also investigate the affairs of the following: (i) any other body corporate which is or was at the relevant time, the Co.'s subsidiary or holding Co. or a subsidiary of its holding Co. or a holding Co. of its subsidiary; (ii) any other corporate body which is or was at the relevant time, managed by common managing agents or secretaries and treasurers or by one who is or was at the relevant time an "associate" of the Co.'s managing agents or secretaries and treasurers or by one, of whom the Co.'s managing agents or secretaries and treasurers were an "associate"; (iii) any other corporate body which is or was at the relevant time managed by the Co. and (iv) a person who is or was at the relevant time managing agent or secretaries and treasurers of the Co. or their "associate". The Inspector may and shall, if required by the Central Government, make *interim reports* and on conclusion of the investigation, a *final report* to the Central Government (written or printed as directed) (s. 241). If it appears to the Central Government on a report under s. 241, that a person, in relation to the Co. and other bodies whose affairs have been investigated as above, has or have been guilty of a criminal offence, it may prosecute such person or bodies. The Co. and the other bodies, their officers and agents [within the meaning of s. 240(6)] shall give all assistance to the Central Government for the aforesaid purposes (s. 242). On the Inspector's Report, if the Central Government thinks it expedient that the Co., other body corporate, or the managing agents, secretaries and treasurers or associate (being bodies corporate) whose affairs were investigated, should be wound up (the said bodies being also liable to be wound up), it may authorise any person to petition to the Court, on behalf of the Central Government for winding up the said body, on the ground of it being just and equitable to do so or to make an application under s. 397 or s. 398 (relief against oppression and against mismanagement) or both (s. 243).

Damages or Property: Under s. 244, if on Inspector's Report it appears to the Central Government that in public interest, proceedings should be started by the Co. against bodies proceeded against under s. 239(a), (b) and (c), to recover damages for fraud, misfeasance or other misconduct in connection with the promotion, formation or management of such bodies or to recover any property belonging to them which is wrongfully retained or misapplied, the Central Government may itself begin such proceedings in Co.'s name.

Power to investigate Ownership of Company: Under s. 247, where it appears to the Central Government that there is good reason to do so, the Central Government may appoint Inspector to investigate and report as to the membership and other matters relating to a Co. for determining the true persons: (i) who are or have been financially interested in the success or failure (real or apparent) of the Co. or (ii) who are or have been able to control or materially influence the policy of the Co. The Central Government may define the scope of the investigation with regard to matters and period and may limit investigation to particular shares and debentures. The Inspector's powers, subject to the terms of appointment, shall extend to circumstances suggesting any arrangement or understanding (whether legally binding or not) observed or likely to be observed in practice with regard to relevant matters. His powers shall also extend, in the above behalf, to the investigation of the ownership of shares of existing as well as past managing agent, secretaries and treasurers (if body corporate) and as to the

persons who are or were in management or control thereof, and if they are or were a firm, of persons who are or were in management and control thereof as partners or otherwise, and of their interest therein and in all cases, to the investigation of persons who are or were entitled to share or interest in the remuneration payable to such managing agents or secretaries and treasurers.

Power to require Information as to Persons interested in Shares or Debentures or interest in Managing Agency, etc.: S. 248 provides that where it appears to the Central Government that there is good reason to investigate the ownership of any shares or debentures of a Co. or a body corporate which acts or has acted as the managing agent or secretaries and treasurers of a Co. and that it is not necessary to appoint an Inspector for the purpose, the Central Government can call upon persons whom it reasonably believes, (i) to be or have been interested in those shares and debentures and/or (ii) to act or have acted as legal adviser or agent with regard to the same, or someone interested therein, to give to the Central Government all information that they can reasonably give as to the present and past interests in the said shares and debentures, of the names and addresses of the persons so interested and of persons who act or have acted on their behalf with regard to the same.

A person shall be deemed "to be interested" in any share or debenture (i) if he has power to acquire or dispose them of or to vote in respect thereof, (ii) if consent of that person is necessary for the exercise of any rights of other persons interested therein or (iii) if other persons interested therein can be required or are accustomed to exercise their rights therein according to his directions.

Similar power is also given to the Central Government on good reason, to obtain information regarding the ownership of any interests in a firm which acts or has acted as the managing agent or secretaries and treasurers of the Co., as regards the present and past interests held in the firm, the names and addresses of the persons interested and of persons who act or have acted on their behalf in relation thereto. Penalties are provided for breach of the above provisions.

Investigation with regard to "Associateship" with Managing Agents: Under s. 249, when any question arises whether any corporate body, firm or individual is or is not an "associate" of the managing agent or secretaries and treasurers, and the Central Government thinks that there is "good reason" to investigate the question, the Central Government may either (i) appoint an Inspector for the purpose or (ii) require any person reasonably appearing to be in position to give relevant information to give the same to the Central Government on specified matters. In case an Inspector is appointed, provisions of s. 247 (see *ante*) and in the other case, of s. 248, with necessary modifications shall apply.

Power to impose Restrictions on Shares and Debentures: S. 250 provides that where in connection with investigations under ss. 247, 248 and 249, there appears to the Central Government a difficulty as regards finding out relevant facts about any shares (issued or to be issued) or debentures and that the difficulty arises on account of the unwillingness of the persons concerned to assist the Central Government in their said investigation, the Central Government may order that, until further orders, (i) any transfer of the said shares or debentures shall be void, (ii) that the same shall not be issued and that any issue thereof or transfer of any right to be issued therewith shall be void, (iii) that no voting rights shall be exercised therewith, (iv) that no further shares shall be issued in right of those shares or in pursuance of any offer made to the holder thereof and that any issue or transfer of a right to be issued therewith in contravention of the above shall be void, (v) that no payment shall be made by the Co. in respect of the said shares and debentures, by way of dividend or capital or otherwise except in liquidation. Any person aggrieved by placing of such restriction or refusal of the Central Government to raise the same, may apply to the Court and the Court may by order, if it thinks fit remove the same. Restrictions may be removed by the Central Government or the Court with qualifications.

Any person knowingly disposing of any shares or rights annexed thereto or debentures or voting or appointing proxies to vote in respect thereof, while the same are under restrictions as above, and any person failing to give notice of the said restrictions to any transferee thereof, are punishable with imprisonment or fine or both. The Co.

also issuing shares in contravention of the restrictions is liable to a fine along with officer in default. Prosecution under the sec. can only be with the consent of the Central Government.

Savings as regards Legal Advisers and Bankers: Nothing in ss. 234-250 however shall require (i) any legal adviser to disclose privileged communications made to him as such, by his client, except the latter's name and address, (ii) any banker of the Co., body corporate, managing agent, secretaries and treasurers or of other persons mentioned in those secs. to disclose the affairs of any other client except the above (s. 251).

Prevention of Oppression

In order to prevent oppression of a minority by a majority of shareholders and to prevent mismanagement of the Co.'s affairs, two classes of powers are now created by the present Act under ss. 397-409. One class of powers are vested in the Court (ss. 397-407), another class of powers are vested in the Central Government (ss. 408-409).

Who can apply: Under s. 399, in case of a Co. having share capital (i) not less than 100 numbers or (ii) not less than 1/10th of the total number of members (which-ever is less) or (iii) a member or members holding not less than 1/10th of the issued share capital of the Co., provided in all the three cases, all calls and other sums due on their respective shares have been paid, can apply for relief under the sec. In case of a Co. not having share capital, 1/5th of the total number of members can similarly apply. Joint holding of shares is to be counted as one member. When members are entitled to make an application as above, any one or more of them, after obtaining the written consent of the requisite number, can make an application under the sec. on behalf of themselves and others. (iv) The Central Government also can authorise a member or members to make the application under the sec., though the above requirements as to the number requisite is not satisfied. The Central Government before giving such authority may demand sufficient security from the members authorised. (v) Under s. 401, the Central Government can itself make an application under the sec. or authorise any person to make the same.

Application, when lies: Under s. 397, where any member of a Co. complains that the affairs of the Co. are being conducted in a manner oppressive to any member or members (including one or more of themselves), and the Court is of opinion that (a) the Co.'s affairs are being conducted in such manner as aforesaid, and (b) that a winding up order would unfairly prejudice such member or members but (c) that otherwise, the facts would justify a winding up order as being just and equitable, the court may make such order as it thinks fit, with a view to bringing to an end the matters complained of. (ii) Where, under s. 398, any members of a Co., complain that (a) that the affairs of the Co. are conducted in a manner prejudicial to the interests of the Co. or (b) that a "material change" has taken place "in the management and control of the company" and that thereby it is likely that the affairs of the Co. will be conducted in a manner prejudicial to the interests of the Co., and the Court is of opinion that the affairs of the Co. are being conducted as aforesaid or by reason of the "change in the management and control", are likely to be conducted as aforesaid, the Court "may make such orders as it thinks fit", in order to bring to an end or preventing the matters complained of or apprehended. "Change" in the management and control mentioned above, includes an alteration in the Board of Directors, or managing agents, secretaries and treasurers, as also in the constitution or control of the managing agents, firm or Co. It also includes "change" in the ownership of the Co.'s shares or membership (where the Co. has no share capital). It does not include, however, a change brought about by or in the interest of any creditors (including debenture-holders or of any class of shareholders of the Co.).

Powers of Court

Under ss. 397 and 398, the Court has power to "make such order as it thinks fit" to end or prevent the matters complained of or apprehended. In particular, under s. 402, it may by its order provide for (i) the regulation of the Co.'s affairs in future, (ii) the purchase of shares or interests of some members by the other members or the Co., and in case of such purchase, for the consequent reduction of capital, (iii)

the termination, modification or setting aside of any agreement (however arrived at) between the Co. and the managing or other director, managing agent, secretaries and treasurers, or manager, on such terms as may be just and equitable. The Court, under the above secs., has power, also to terminate, modify or set aside, any agreement between the Co. and any person other than above. In such a case, however, prior notice must be given to the person concerned and further, the agreement cannot be modified except with the consent of the party. The Court has power, also to provide for any other matter which it deems just and equitable to provide for. Under s. 403, the Court has power to make such interim orders as it may think fit, for regulating the conduct of the Co.'s affairs on the application of any party to the proceedings. Wide powers of a punitive nature are also given to the Court under s. 406, which makes ss. 539-544, with modifications, specified in Sch. XI, applicable to applications made under the above secs. These powers include powers to punish for not keeping proper books of account (s. 541), for fraudulent conduct of the Co.'s business (s. 542), for assessing damages against delinquent director and others under s. 543, for falsification of the Co.'s books (s. 539) and for fraudulent transfers of Co.'s property (s. 540).

The powers of the Court under the above secs. are unlimited. It can pass any order or orders which may appear to it necessary, just and equitable, to set right the distempers affecting the management of the Co.'s affairs in any given case. In fact, the Court may impose upon the parties whatever settlement it considers a fair and reasonable solution of the difficulty.

S. 404 further provides that where an order made under the secs. involves an alteration of the Memo. or Articles of the Co., the Co. shall have no right to alter the same in future without leave of the Court. Certified copies of such orders must be filed with the Registrar within 15 days of their making, punishment for default being a fine (upto Rs. 5,000). Where an order of the Court under the above secs. involves the termination of any of the agreements mentioned before, such termination shall not give rise to any claim for damages against the Co. for loss of office or otherwise. The managing or other director, managing agent, secretaries and treasurers, and manager, whose agreements are terminated or set aside as aforesaid and any then existing or subsequent "associate" of such managing agent or secretaries and treasurers, shall, for a period of 5 years thereafter, not be capable of being appointed to any of the above offices or act as such officers, without leave of the Court. Contravention of the above prohibition, on the part of any of the above persons and/or their partners or directors (if the managing agent or secretaries and treasurers are a firm or a corporate body), is punishable with imprisonment and fine or both (s. 407). No leave shall be granted by the Court to any of the above persons under the sec. without prior notice to and without hearing the Central Government.

Powers of the Central Government

Two special powers are conferred on the Central Government to stop mismanagement of the affairs of a Co. under ss. 408 and 409 of the Act. Under the first sec., the Central Government has power to appoint two nominees of its own to be additional directors of the Co. for a period not exceeding 3 years at one time if it thinks necessary to do so, after proper inquiries, to prevent affairs of the Co. being conducted in a manner oppressive to any members or prejudicial to the interests of the Co. An application by 200 members or by shareholders holding 1/10th of the total voting power of the Co. is necessary before the Central Government can exercise the above power. The Central Government on such application has power to make interim appointment of two members of the Co. as additional directors till new directors are appointed by it as above. The Central Government may instead of acting as above, direct the Co. to amend its articles by adopting the system of proportional representation under s. 265, as regards appointment of directors, within a specified time. Additional directors appointed as above, are not to be counted in calculating 2/3rds or any other number of directors.

Under s. 409, where managing or other director, managing agent or secretaries and treasurers, complain to the Central Government, that as a result of a "change in the ownership of the shares" of the Co. which has taken, or is about to take place, a change in the Board of directors is likely to take place, which would prejudicially affect the

Co.'s affairs, the Central Government, after proper inquiry and if it thinks just and proper, direct that no resolution passed or action taken after such complaint, shall effect a change in the Board, unless such change is confirmed by the Central Government. The Central Government can pass such interim orders in the above behalf as may be necessary. The above provision does not apply to private Co., unless subsidiary of a public Co.

Powers under the Constitution : It has been held by the Supreme Court that under Art. 19(5) of the Constitution Act, the State has the right to restrict the rights of management of a Co. by its shareholders by appointing directors, in order to secure the supply of a commodity essential to the community and to prevent serious unemployment amongst a section of the people (r). Similarly, under Art. 31 of the Constitution Act also, it has been held by the Supreme Court that the State has power to enact laws acquiring any Co., owning a commercial or industrial undertaking, for public purposes, on payment of just compensation (s). The amount of compensation, however, is no longer justiciable by reason of Constitution (Fourth Amendment) Act of 1955.

DIRECTORS

Position of Directors : Directors are called by various names. The exact legal position of the directors of a Co. is difficult to define. They have been called "trustees" and they are trustees for some purpose and to some extent for the company, e.g. as regards their power of approving transfers, issuing and allotting shares, making calls, receiving moneys in advance of calls, forfeiting shares and generally in the employment of the funds of the Co. Directors are agents for the Co. also, to some extent. Thus where they make contracts for the Co., they are not personally liable thereon unless they have personally taken the liability upon themselves.

The best way to describe their position is to say that they stand in a fiduciary position towards the Co. in regard to powers conferred on them by the articles (t).

Appointment of Directors : S. 252 provides that every public Co. (and every private Co., which is a subsidiary of such Co.) shall have at least 3 directors. Every private Co. (other than the above), shall have at least 2 directors. Directors are collectively called the "Board of Directors", or the "Board". No body corporate, firm or association can be appointed a director of a public or private Co. Only an individual can be so appointed (s. 253). Unless the articles otherwise provide, subscribers to the Memo. (who are individuals), shall be deemed to be the directors of the Co. till directors are duly appointed by the Co. in general meeting (s. 254). Generally, the articles name the first directors, sometimes, as reg. 64 of Table A lays down, articles may also provide that both the number and the names of the first directors shall be determined in writing by the subscribers to the Memo. or a majority of them (u). In absence of any such provisions, the provisions of s. 254 will be operative.

Rotational Directors : S. 255 provides that not less than 2/3rds of the total number of directors of a public Co. (and of a private Co. which is subsidiary thereof), shall be persons whose period of office is liable to terminate by retirement by rotation. The aforesaid directors shall be appointed by the Co. in general meeting, except where otherwise provided by the Act. The remaining 1/3rd of the total number of directors shall, in case of the above named Co.s, be appointed by the Co. in general meeting, subject, however, to the articles (if any). In case of private Co. other than above, all the directors, subject to the articles (if any), shall be appointed by the Co. in general meeting. Subject to the Act, any person, other than a retiring director (for which see seq.), shall be eligible for appointment as director, at any general meeting, if he or some member proposing him, leaves at the Co.'s office, not less than 14 days before such meeting, a written notice signed by such person, signifying his intention to stand as or to propose such person as a candidate for such office. This, however, does not apply to a private Co. (which is not a public Co.'s subsidiary) (s. 257). Notice that

(r) Chiranjitlal v. Union of India (1951) S.C. 41.

(s) Dwarkadas v. Sholapur Sp. & W. Co. (1954) S.C.A. 132.

(t) City Equitable Fire Ins. Co. (1925) 1 Ch. 407.

(u) John Morley Building Co. v. Barnes (1891) 2 Ch. 386.

s. 408 of the Act gives power to the Central Government to appoint directors, in cases where it is necessary to do so, in order to prevent oppression, etc. Similarly, s. 409 gives power to the Central Government to prevent a change in the constitution of the Board where such change is likely to prejudice the Co.'s interests by reason of change of control involved therein.

Ex-Officio or Nominated Directors: S. 255 permits 1/3rd of the total number of Directors of a public Co. (and of a private subsidiary thereof) to be appointed by the relevant parties on a non-rotational basis. This quota may be filled up, if the articles so authorise, by parties other than the shareholders, if they are entitled to do so under their special agreements, e.g. by managing agents or debenture-holders. As regards these "ex-officio directors", it should be noticed that under s. 377, the managing agents have now the power to appoint a maximum of two directors only, whatever the total number of directors above five may be and one director only, where the total number of directors does not exceed five.

Private Companies (other than those mentioned above), are free to appoint all directors on a non-rotational basis under the sec. S. 377 gives power to the managing agent at any time to remove his "ex-officio directors" and appoint others in their places on such removal or resignation or vacation. The same sec. further provides that where at the commencement of the Act, managing agents have appointed more than their above authorised number of directors in any Co., the managing agents shall decide before the expiry of one month of the commencement of the present Act, which of them shall continue to hold office. If no such choice is made within the prescribed period, all their directors shall be deemed to have vacated office.

Retirement by Rotation and Re-election of Directors

S. 256 provides that in case of a public Co. (and a private Co. which is its subsidiary), 1/3rd of the directors who are liable to retire by rotation (and if their number is not three or a multiple of three, the number nearest to 1/3rd), shall retire from office at the first annual general meeting, after the general meeting at which the first directors are appointed under s. 255, and thereafter, a similar proportion shall retire at each subsequent annual general meeting. The directors to retire shall be those who have been longest in office. As between persons appointed directors on the same day, the question shall be decided by lot, in absence of or subject to any agreement between them. The Co. can fill up the vacancy at the general meeting at which a director retires as above, by appointing him or any other person thereto. If his place is not filled up as above and the meeting does not expressly resolve that such vacancy shall not be filled up, the meeting shall stand adjourned, till the same day, next week at the same time and place (if the day is a holiday, till the next day thereafter, at the same time and place). If at the adjourned meeting, the vacancy is not filled up (and the meeting has not resolved expressly not to fill up the vacancy), the retiring director shall be deemed to be reappointed at such adjourned meeting, provided that he shall not be deemed to be reappointed (i) if at that meeting or any previous meeting, a resolution for reappointing him has been put to the meeting and lost; (ii) if such person by writing addressed to the Co. or Board has declined reappointment; (iii) if he is not qualified or is disqualified; (iv) if under the Act, a resolution, whether ordinary or special, is required for his appointment or reappointment; (v) if a resolution for appointment of director is passed under s. 263 but it is void and (iv) if he is superannuated under s. 280(3). Where a director retiring by rotation as above is liable to retire by superannuation also, his retirement shall be considered to be one by rotation.

Increase or Decrease in the Number of Directors: S. 258 provides that subject to the provisions of s. 252 (minimum number of directors), s. 255 (rotation of directors) and s. 259 (sanction of Central Government for increasing number of directors), a Co. may, in general meeting, by *ordinary resolution*, increase or reduce the number of directors within the limits fixed by the articles. Under s. 259, when such increase in case of public Co.s (and private Co.s which were subsidiaries thereof) in existence on 21st July 1951, is beyond the permissible maximum under their then existing articles, and in case of Co.s such as above, coming into existence after that date, where the increase is beyond the permissible maximum fixed under their Memo. and articles, the same shall be void and of no effect unless approved by the Central Government.

Restrictions on Appointment of Directors

(i) Managing Agents' powers to appoint ordinary Directors: S. 261 provides that where in case of a public Co. (and a private subsidiary thereof), the managing agent is authorised by articles or by agreement to appoint director on the Board, the following persons shall not be appointed as rotational directors, except by a *special resolution* passed by the Co. in that behalf. *Special Notice* shall be required for any resolution appointing or reappointing such person as director. The notice given to the Co. of such resolution and the notice thereof given by the Co. to the members, shall set out the reasons which make such resolution necessary. The prohibited persons are: (i) any officer or employee of the Co. or its subsidiary; (ii) any person holding an office or place of profit under the Co. or its subsidiary (persons exempted by s. 314 being excluded); (iv) where such office or place of profit as is mentioned in (iii), is held by a firm, a partner or employee of the firm; (v) where such office or place of profit as is mentioned in (iii) is held by a private Co., a member, officer or employee of such Co.; (vi) if such office or place of profit as mentioned in (iii) above is held by a body corporate, any officer or employee of the same; (vii) any person entitled to share in the remuneration of the managing agent; (ix) any "associate", employee or officer of the managing agent, and (x) any person who is an officer or employee of a body corporate (or subsidiary thereof), under the management of the managing agent or a person holding office or place of profit in such corporate body or subsidiary thereof (persons exempted under s. 314 being excluded). A director holding office at the commencement of the Act in contravention of the above, is not affected and he shall continue to hold office till the next annual general meeting of the Co. [This sec. deals with appointments as regards the two-thirds quota of directors who are liable to periodical retirement by rotation under s. 255 of the Act.]

(ii) No resolution for joint appointment: S. 263 provides that in case of a public Co. (and a private Co., subsidiary thereof), a motion shall not be made for the appointment of two or more persons as directors, by a single resolution, unless a resolution sanctioning such course has been passed unanimously at the meeting, beforehand. For the above purposes, a motion for approving a person's appointment or nominating a person for appointment shall be treated as a sanction for his appointment. Any resolution, passed otherwise than as above, shall be void, whether objection thereto has been taken or not. Such a resolution, if passed however, will have the effect of preventing the automatic reappointment of a retiring director under s. 256(4).

(iii) Written consent of director necessary: Under s. 264, no person (other than a retiring director), shall be appointed director, unless he, by himself (or by an agent authorised in writing), has filed with the Registrar a consent in writing to act as such. The above provision does not apply to private Co. (other than subsidiary of a public Co.).

(iv) Proportional representation on Board: A very important right is now for the first time created, so far as appointment of directors is concerned by s. 265 of the present Act. The sec. provides that notwithstanding anything contained in the Act, the articles of a Co. may provide that the appointment of not less than 2/3rds of the total number of directors of a public Co. (or a private Co., subsidiary thereof), shall be according to the principle of *proportional representation*, either by the single transferable vote or by a system of cumulative voting or otherwise; such appointments being made once in three years, and interim casual vacancies being filled up according to s. 261 with necessary modifications.

(v) Qualification shares must be taken up: Under s. 266, a person shall not be capable of being appointed director by articles nor shall his name be mentioned as a director or proposed director in a prospectus issued by or on behalf of a Co. or intended Co., or in any statement in lieu of prospectus filed with the Registrar, unless, before registration of articles, issue of prospectus, or filing of statement, he has, by himself (or his agent authorised in writing), (i) signed and filed with the Registrar consent in writing to act as such director and (ii) either signed the Memo. for his qualification shares or taken his qualification shares from the Co. and paid or agreed to pay for them or signed and filed with the Registrar an undertaking to take from the Co. his qualification shares and pay for them or has filed with the Registrar an affidavit stating that such qualification shares are registered in his name. Filing the above undertaking

with the Registrar has the same effect as if he had signed the Memo. for such shares. The share qualification referred to above refers only to share qualification within a period of time determined by reference to the time of appointment. The sec. does not however apply to (i) a private Co., (ii) a Co. not having share capital, (iii) a Co. which was a private Co. before becoming a public Co. and (iv) to a prospectus issued one year after the Co. is entitled to commence business.

(vi) Disqualified persons not to be appointed : Certain persons are statutorily made disqualified for being appointed directors under s. 274. They are: (i) a person found by Court to be of unsound mind (the finding being in force); (ii) an undischarged insolvent, (iii) a person who has applied for adjudication and whose application is pending; (iv) a person convicted by an Indian Court and sentenced to imprisonment for 6 months or more and in whose case 5 years have not elapsed since the sentence; (v) if he has not paid any call on his shares (held by him alone or jointly with others) for more than 6 months after date fixed for payment of the same; (vi) if a disqualification order has been passed against him by a Court under s. 203 and is in force, unless leave of the Court has been obtained under the same. The Central Government by Notification has power to remove disqualifications under (v) and (vi) above, generally or with regard to special Co.s Private Co.s (other than subsidiaries of public Co.s), may, by their articles, add to the above grounds of disqualification. Under s. 202, if an undischarged insolvent discharges any of the functions of a director (or acts or discharges any of the functions of managing agents, secretaries and treasurers or manager) or directly or indirectly takes part in or is concerned in the promotion, formation or management of a Co., he shall be punishable with imprisonment or fine or both. "Company" here includes an unregistered Co. as well as foreign Co. having an established place of business in India. Similarly, s. 203 provides that (i) where a person is convicted of an offence in connection with the promotion, formation or management of a Co., or (ii) where in the course of winding up of a Co., it appears that (a) a person has been guilty of an offence under s. 542 (whether convicted or not), or (b) has been otherwise guilty as "officer" of the Co. of any fraud, misfeasance or breach of duty with relation to the Co., the Court may order that such person shall not without leave of the Court be a director of or in any way be concerned with or take part in the promotion, formation or management of a Co., for a period not exceeding 5 years. The Court as regards (i) includes the convicting Court and the Court having jurisdiction to wind up the Co. and as regards (ii) the Court having jurisdiction to wind up the Co.

(vii) Numerous Directorships prohibited : A restriction is now placed on the number of directorships a person can hold. Under s. 275, no person can hold more than 20 directorships of Co.s at the same time. A person holding more than the above number of directorships at the commencement of the Act, must within 2 months thereafter (i) choose not more than 20 Co.s of which he wishes to remain director, (ii) resign from the rest, and (iii) intimate his choice, to each of the Co.s of which he was director, to the Registrar having jurisdiction over each, and to the Central Government. Resignation will be effective from the date of the dispatch thereof. No person shall act as director of more than 20 Co.s after two months of the commencement of the Act or after despatching his resignation as above (s. 276). Under s. 277, if a person holding 20 directorships is appointed director of another Co. after the commencement of the Act, such appointment shall not take effect, unless within 15 days of such appointment, he vacates his office as director in any of the other Co.s and if he fails to do so, the appointment shall be void on expiry of such period. If a person holding 19 or less directorships is, after commencement of the Act, appointed director of other Co.s, he must choose from them, so that the total does not exceed 20. The choice must be made within 15 days of the new appointment, otherwise the appointments would be void. S. 278 provides that in calculating the above number of 20, the following Co.s shall be excluded: (i) private Co. (not being subsidiary of a public Co.), (ii) unlimited Co., (iii) a Co. not carrying on business for profit or which prohibits payment of dividend, (iv) a Co. in which the person is only an "alternative director". Exemption with regard to the above Co.s is to continue for 3 months after they have ceased to be such. Penalty for violation of the above provisions is a fine (upto Rs. 5,000 for each of the Co.s over 20) (s. 279).

(viii) Age bar: A new age bar is now introduced by s. 280 of the Act. Under the sec., a person 65 years in age and over shall not be appointed director of a public Co. (or of a private subsidiary Co. thereof). Such director shall vacate office at the conclusion of the annual general meeting, commencing next after he attains the above age. As regards such persons acting as directors at the commencement of the Act, they shall vacate office after the conclusion of the third Annual General Meeting held after commencement of the Act, if they have completed 65 before commencement of such meeting. Where such a person retires, the provisions for automatic reappointment of directors in default of appointment shall not apply but if his vacancy is not filled at the aforesaid meeting, it shall be filled up as a casual vacancy, under s. 262. Under s. 280, the above disability as regards age shall not apply if the Co. in general meeting resolves specifically that the bar of age-limit shall not apply to any particular director. Special notice (under s. 190 *ante*) is necessary for such resolution, otherwise the resolution will be void. Notice to the Co. and to the members of the Co. of such resolution must state the age of the person concerned. A person appointed or to be appointed director, who has attained 65 years (or less age as provided by the articles), must, under s. 282, give notice of his age to the Co. Such notice will not be necessary as regards reappointment, if it has been already given with regard to such person during or in connection with a previous appointment. A person failing to give such notice or acting as director after attaining such age in violation of the above, is liable to a fine.

Additional Directors: S. 260 provides that notwithstanding the provisions of ss. 255, 258 and 259, the Board of Directors shall always have power, if authorised by the articles, to appoint additional directors, but in such cases: (i) the total number of directors shall not exceed the maximum fixed by the articles and (ii) such additional directors shall hold office upto the date of the next annual general meeting of the Co. If the articles so provide, however, such persons may be eligible for appointment as directors at such meeting, after the meeting, if necessary, has increased the number of directors (reg. 72, Table A).

Alternate Directors: Under s. 313, the Board shall have power, if authorised by the articles, or a resolution of the Co. at general meeting, to appoint alternate director during the absence of a director for not less than 3 months from the State in which the Board meetings are ordinarily held. The alternate director shall vacate office if and when the original director returns to the State in question. If the original director's term of office expires before he returns to the said State, the rule as regards automatic re-appointment of retiring director shall apply to the original and not to the additional director.

Casual Vacancies: S. 262 provides that in case of a public Co. (and subsidiary private Co. thereof), a casual vacancy in the panel of directors appointed by the Co. in general meeting shall, subject to the articles, be filled up by the Board at a Board meeting. The person so appointed shall hold office only upto the date to which the director in whose place he has been appointed, would have held the office. "Casual vacancy" means a vacancy caused by the termination of the term of office of a director, otherwise than in its normal course.

Managing Director

Under s. 267, after the commencement of the present Act, no Co. shall appoint or continue in appointment, as managing or whole-time director, a person (i) who is an undischarged insolvent or has been at any time adjudged insolvent, (ii) who suspends or has at any time suspended payment of debts or compounds or has at any time compounded with creditors, or (iii) who is or has been at any time convicted by an Indian Court of an offence involving moral turpitude. The sec. however does not apply to a private Co. (unless subsidiary of a public Co.).

Certain additional restrictions on appointment of managing directors are placed by ss. 316-317. These restrictions do not apply to private Co.s (unless subsidiaries of public Co.) (s. 315). They are as follows: (i) after the commencement of the Act, no Co. shall employ or appoint any person as a managing director, if he is already a managing director or manager of another Co. He can be appointed or employed such managing director of a Co., though already a managing director or manager of one other Co., only

if such employment or appointment is made with the unanimous consent of all the directors of the former Co., present at a meeting of the Board, of which meeting and of the resolution to be moved thereat, specific notice is given to all directors in India. If at the commencement of the Act, a person is a managing director of more than two Co.s, he shall, within 1 year thereof, choose, of which two of them he wishes to remain managing director. The provisions of s. 276, cl. (i) (b) and (c) and cls. (ii) and (iii) as regards making a choice shall apply with necessary modifications in such case (s. 316). The Central Government however may permit a person to be appointed managing director of more than two Co.s if satisfied that for the proper working of the same Co.s as a single unit, a common managing director is necessary. (ii) No person, after the commencement of the Act, shall be employed or appointed managing director for more than 5 years at a time. All existing managing directors shall be deemed to vacate their offices after five years of commencement of the Act (unless their terms expire earlier). Re-employment, reappointment and extension of the term of managing directors for periods not exceeding 5 years on each occasion, are not prohibited but these must be sanctioned, only within the last 2 years of their existing terms (s. 317). Notice that no exemption is made in cases of technical or consulting directors even.

Where in case of an existing public Co. (and a private Co., subsidiary thereof), a managing director or a whole-time director is appointed for the first time after the commencement of the Act and in case of other Co.s, after 3 months of their incorporation, where a managing or whole-time director is appointed, if such appointment is not approved by the Central Government, the same shall be void and of no effect, in so far as disapproved by the Central Government (s. 269). Similarly, any amendment of any provision with regard to the appointment or reappointment of a managing or whole-time director, or a director not liable to retire by rotation, shall, in case of a public Co. (and a private Co., subsidiary thereof), be of no effect, unless approved by the Central Government and shall become void so far as not so approved. The provision may be contained in the Memo. or the articles or in any resolution of the Co. or Board or in any agreement with the Co. (s. 268).

Where a Co. appoints one of its directors as the managing director for a term of years, the contract is governed by the general rules of an employer and employee. Thus the agreement would end, if the managing director were to die or become permanently incapacitated. The Co. would also have the right to dismiss him from his office on the ground of misconduct, e.g. embezzlement or disgraceful conduct leading to conviction for an indictable offence. Further, the directorship is an integral and necessary element in the composite office. On his ceasing to be a director, he would *ipso facto* also cease to be a managing director. The Co., however, cannot remove him from his office during the term, without some legal excuse. In this connection, it is to be observed that the usual power given to a Co. by its articles, to dismiss a director, cannot be invoked to justify a dismissal without any just or legal cause nor, as has been recently held by the House of Lords, can such a dismissal be justified by an alteration of articles of the Co. (v).

Quasi-Directors : The Act has brought within its purview a new set of persons, who though they do not formally occupy the position of directors of a Co., still hold such power of control over the Co.'s affairs and the management thereof, that they may be truly and faithfully regarded as, and placed almost in the same category as, formally appointed directors of a Co. These persons are described as *persons "according to whose directions or instructions the directors of a Co. are accustomed to act"*. The cases envisaged are those where the directors of a Co. have such controlling interest over a private or other limited Co. that though the latter Co. has directors of its own, yet they have to be guided by and have to carry on the business of the latter Co. according to the dictates of the other directors. Very often, the directors of such private and other Co.s are nominees of the other directors. Directors of major Co.s can thus control the management and administration and destinies of a number of other minor Co.s which though technically not "subsidiaries" of the major Co., are still under such subservience and control of the directors of the major Co. as to be truly regarded as their creatures or creations. Various provisions are contained in the Act for persons who occupy such

position with regard to a Co. that, without being formal directors thereof, they are still able to control the destinies of another Co. and whom we may well call *quasi-directors*.

Share Qualification for Directors

The Act does not provide that every Co. must require a certain number of qualification shares to be held by a director, before being eligible for directorship (*w*). A share qualification however is generally always provided by the articles, for directors. In absence of such provision, Reg. 66 of Table A now provides that the qualification of a director shall be the holding of one share of the Co. Every director is bound to obtain his qualification shares (if any) within 2 months after his appointment, if he has not already obtained the same. Articles providing that a director shall obtain his qualification shares before his appointment, or within less than 2 months thereafter, are void. In no case shall the nominal value of qualification shares exceed Rs. 5,000, except where the qualification is one share and the nominal value thereof exceeds the above amount. The bearer of a share warrant shall not be regarded, for the above purposes, as a holder of the shares represented thereby (s. 270). Every director (unless he is a technical director or a State or Central Government director), shall within 2 months of his appointment, or the commencement of the Act (if already a director), file with the Registrar a declaration specifying the qualification shares held by him (s. 271). If after the above period of 2 months, a person acts as director without holding the qualification shares, he is liable to a fine (upto Rs. 50 per day, he acts as such director) (s. 272). *The above provisions do not apply to a private Co., unless subsidiary of a public Co. (s. 273).* Further, as s. 283 provides, the office of the director shall be automatically vacated, if he does not obtain his qualification shares within the above period or ceases to hold the same at any time thereafter.

Vacation of Office by Director

S. 283 provides that the office of director shall be automatically vacated: (i) if the person fails to obtain the qualification shares (if any) within the time fixed by s. 270 or at any time ceases to hold such shares; (ii) if found a lunatic under order of Court; (iii) if he applies to be adjudicated insolvent; (iv) if he is adjudged insolvent; (v) if convicted by an Indian Court and sentenced to imprisonment of not less than 6 months; (vi) if he fails to pay call on shares held by him alone or jointly with others, within 6 months of the last day for payment; (vii) if he "absents" himself from 3 consecutive meetings of the Board or from all meetings of the Board, for a continuous period of 3 months (whichever is longer), without obtaining leave of absence from the Board; (viii) if he contravenes the provisions as regards disclosure of interest under s. 299; (ix) if he or his firm or any private Co. of which he is director accepts a loan, security or guarantee for loan from the Co., in contravention of s. 295; (x) if he becomes disqualified by an order of the Court under s. 203 or (xi) if he is removed by the shareholders under s. 284. As regards (iii), (iv) and (x) above, the disqualification shall not become operative till 30 days after date of adjudication or sentence; in case of appeals from the same within the said period, till 7 days after disposal of appeal, and in case of a further appeal within the said period, till 7 days after its disposal. A private Co. (which is not a subsidiary of a public Co.), can, by its articles, add other grounds than above, for vacation of office of director.

Vacation of Office: The provisions of s. 283 have to be read as supplemented by those of s. 314, under which, no director or a partner or relative of such director, no firm, in which such director or relative is a partner, no private Co. of which such director is a director or member, and no director, managing agent, secretaries and treasurers or manager of such private Co., shall hold any office or place of profit (with certain exceptions), under the Co., or its subsidiary, except with previous consent of Co. given by a special resolution. If any of the above persons holds such office or place of profit without the sanction of such special resolution, cl. (2) of s. 314 provides that the director in question shall be deemed to have vacated his office as director, from the first day the contravention occurs.

Removal of Director

S. 284 provides that a Co. may, by *ordinary resolution*, remove a director from office before his term has expired. The above, however, does not apply to a director appointed by the Central Government under s. 408 or to a director of a private Co. holding office for life on 1st April 1952, whether he is or is not subject to retirement by age by virtue of articles or otherwise. Similarly, where under s. 265, the Co. has appointed two-thirds of the directors by proportional representation, this provision will not apply. *Special notice* (under s. 190) is necessary for a resolution for removal of a director or to appoint another in his place. On receipt of such resolution, the Co. shall forthwith send a copy thereof to the director concerned and the director shall be entitled to be heard on the resolution, whether a member or not. A copy of written representation (if any), made by, and required to be notified to members by, the director concerned, shall be sent to every member to whom notice of meeting is sent and the fact of such representations shall be specified in the notice, unless received too late. In the latter case, the director in question may require the representations to be read out at the meeting (besides being orally heard himself). Such representations need not be notified, nor copies thereof sent to members, nor the same be read at the meeting, if the Court is satisfied that they are an abuse of the right conferred, for obtaining needless publicity for defamatory matter. In such case, the Director concerned may have to pay costs, though no party to the proceedings.

A vacancy created by the removal of a director as aforesaid can, if he has been appointed in general meeting or by the Board under s. 262 (on a casual vacancy), be filled up at the meeting at which he is removed, provided special notice of such intention is given as above. The director so appointed shall hold office till the date the director removed would otherwise have held office. If the vacancy is not filled as above, it shall be filled up under s. 262 as casual vacancy, except that the director removed shall not be capable of being reappointed. The above provisions do not affect the right (if any) of the director removed, to claim compensation or damages against the Co. for the same, nor the right of the Co. (if any) to remove the director, apart from the sec.

POWERS OF BOARD OF DIRECTORS

General Powers: S. 291 provides that subject to the Act, the Board shall exercise all powers and do all acts and things which the Co. is authorised to do, *excepting* those powers and acts, which either by the present Act or any previous Companies Acts or by the Memo. or articles or otherwise, are required to be exercised and done by the Co. in general meeting. The exercise of the above powers by the Board shall be subject to the provisions in that behalf contained in this or any other Act or the Memo. or articles or in any regulations made thereunder (not inconsistent therewith) or by the Co. in general meeting.

(i) **Certain powers to be exercised by Board only at Board Meeting:** Under s. 292, the following powers can be exercised by the Board, *only* by resolution at Board Meeting: (i) power to make calls, (ii) power to issue debentures, (iii) power to borrow money otherwise than on debentures, (iv) power to invest funds of the Co., and (v) power to make loans. Powers under (iii), (iv) and (v) above can be delegated by the Board, at a meeting, by means of a resolution, to a committee of directors, to the managing director, managing agent, secretaries and treasurers or manager and in case of a banking Co., also to a manager or other principal officer of a branch office. In such cases, however, the resolution must specify as regards (iii), the total amount of permitted borrowing; as to (iv) the total amount permitted to be invested and the nature of the permitted investments; as to (v), the permitted total amount of the loans to be made, the purposes thereof and the maximum amount for each purpose. The Co., in general meeting, shall have power to put restrictions and conditions for the exercise of the above powers by the Board.

(ii) **Powers exercisable only with consent of company in General Meeting:** S. 293 provides that in case of public Co.s (and private subsidiaries thereof), the Board shall not exercise the following powers, except with the consent of the Co. in general meeting. These powers are: (i) power to sell, lease or otherwise dispose of the whole or sub-

stantially the whole of the undertaking or any one or more undertakings of the Co. This however is not to affect the title of an alienee in good faith after exercising due care and caution. It also does not invalidate a sale or lease of any property of a Co. whose business is to sell or lease properties. The resolution of the Co. sanctioning such sale or lease may impose conditions with regard thereto and particularly for the use, disposal and investment of the proceeds of such sale or lease. No reduction of capital however is permissible to the Co. in so imposing conditions except as provided by the Act; (ii) to remit and give time for payment of debt due by a director; (iii) to invest in securities other than trust securities, the sale proceeds of any undertaking of the Co. or of any premises or property used for such undertaking, and without which it cannot be carried on or can be carried on with difficulty or after a considerable time, when such undertaking, property or premises are acquired without the consent of the Co. (i.e. compulsorily acquired) after the commencement of the Act; (iv) to borrow moneys after the commencement of the Act, which together with moneys already borrowed, exceed the paid-up capital of the Co. including its free reserves (i.e. reserves not set apart for any specific purpose). Temporary loans obtained from the Co.'s bankers in the ordinary course of business are not to be considered for the above purpose. Acceptance of deposits from the public by a Banking Co. in the ordinary course of its business, which are repayable on demand, by cheque, draft, or otherwise, shall not be regarded as "borrowing", within the meaning of this clause. Borrowings in excess of the above limits shall not be binding on the Co., unless the lender proves that he made the advance in good faith and without notice that the limits had been exceeded; (v) to contribute after the commencement of the Act, to any charitable, or other funds (not relating directly to the business of the Co. or the welfare of its employees), any sums, the total whereof will exceed Rs. 25,000 or 5 per cent of the average net profits of the Co. during the past 3 years (whichever is greater), in any financial year. Net profits are to be calculated according to ss. 349 and 350.

(iii) **Appointment of Sole Selling Agents:** S. 294 provides that after the commencement of the Act, the Board shall not appoint sole selling agents for any area, except with the condition that such appointment shall cease to be valid if not approved by the Co. in general meeting within 6 months from date of appointment. If the Co. does not approve such appointment, the same shall be void on such disapproval or end of 6 months as the case may be. If before the commencement of the Act, a Co. has appointed sole selling agent for any area for 5 years or more, the appointment shall be placed before the Co. in general meeting within 6 months of the commencement of the Act. If the appointment is made on or after 15th February 1955, the Co. in general meeting may by resolution terminate the appointment forthwith or from a later specified date. If the appointment is made before the aforesaid date, the Co. may terminate the appointment from a date, not less than 5 years from the date of appointment or one year from the commencement of the Act, wherever is later.

(iv) **Loans to Directors:** S. 295 provides that: (1) no Co. shall, without the previous permission of the Central Government, make any loan to (i) any director of the Co. or of its holding Co. or to any partner or relative of such director, (ii) to any firm in which such director or relative is a partner, (iii) to a private Co. of which such director is a director or member, (iv) to any body corporate of which 25% of the voting power is capable of being exercised or controlled by such director or more than one such director together, (v) to any body corporate, whose board of directors, managing director, managing agent, secretaries and treasurers or manager, is "accustomed to act in accordance with the instructions" of the Board or of any director or directors of the lending Co. Providing guarantee or security by the Co. for loans made to the above parties by others is also prohibited, with the same qualifications. The Co. is also similarly prohibited from giving guarantee or security for loans made by the above parties to other persons.

(2) The sec. however does not apply to loans, guarantee or security given by: (i) a private Co. (unless subsidiary of a public Co.), (ii) by a Banking Co., (iii) by a holding Co. to its subsidiary and (iv) by a Co. which is managing agents or secretaries and treasurers of another Co. to the latter.

(3) As regards loans, guarantees and securities given by a Co. which are outstanding at the commencement of the Act and which would have required sanction of the Central

Government if the above sec. had been in force at the time, the Co. must obtain the sanction of the Central Government within 6 months of the commencement of the Act (or within such extended time, not exceeding 6 months as the Central Government may grant), or enforce repayment of the loans made or for which guarantee or security was given.

(4) Persons knowingly acting in contravention of (1) and (3) above, and in particular, the borrowing party, are liable to a fine (upto Rs. 5,000) or imprisonment (upto 6 months); where such loan has been fully repaid, however, no imprisonment shall be given and where it is partially repaid, the imprisonment shall be proportionately reduced.

(5) Persons knowingly contravening (1) or (3) above, are further liable, jointly and severally, to repay the said loan to the lending Co. or to make good the same when the lending Co. has been called upon to pay under the guarantee or security.

(6) No officer of the lending Co. or of the borrowing party (where a body corporate), shall be liable under (4) and (5) above, unless he knew or had express notice at the relevant time that the loan or guarantee or security contravened the provisions of the sec. A loan or advance in the nature of a book debt, made for the purpose of preparing a balance sheet of the Co. (unless it is in fact a loan at its inception), is not within the purview of s. 295 (s. 296). A director acting in contravention of the sec. automatically vacates office under s. 283.

(v) **Sanction of the Board to Contracts in which Director is interested:** S. 297 provides that a director, a firm in which he is a partner and a private Co. of which such director is a member or director, shall not enter into any contract with the Co.: (i) for sale, purchase or for services or (ii) after the commencement of the Act, for underwriting shares or debentures of the Co., except with the "consent" of the Board of directors. Such "consent" must be given by the Board by a resolution at a meeting thereof, and either before the contract is entered into or within 2 months thereafter. If such "consent" is not accorded, the contract shall be voidable at the option of the Board. Contracts to which "consent" has been accorded before the commencement of the Act, are not affected by the above. The above provisions as regards "consent" do not apply to contract for sale, purchase, or supply of materials or services in which either the Co., the director, his firm, partner or Co. regularly trades or does business, provided the value thereof does not exceed Rs. 5,000 in all, in the calendar year comprised in the contracts. The sec. does not prevent a director from taking shares in the Co., though he cannot vote on allotment of such shares to himself (x). He can also subscribe for debentures of the Co. (y).

(vi) **Disclosure where Director interested in Contract with Company:** Under s. 299, every director directly or indirectly concerned or interested in any contract or arrangement proposed to be made with the Co., shall disclose the nature of his interest or concern at a meeting of the Board. In case of a proposed contract or arrangement, such disclosure shall be made at the meeting of the Board, at which the same is first considered by the Board; if the director acquires interest or concern thereafter, this must be done at the next meeting of the Board thereafter. In case of other contracts and arrangements, the disclosure shall be made at the next meeting of the Board, after the director becomes interested or concerned therein. Punishment for breach of the above is a fine.

For the above purposes, a general notice given to the Board, by the director that he is a director or member of a specified body corporate or firm and is to be regarded as interested or concerned in any contract or arrangement with that corporate body or firm entered into after such notice, shall be deemed to be sufficient disclosure. Such general notice will be good till the end of the financial year in which it is given and must be renewed for each subsequent financial year to be effective. Such general notice must be given at a meeting of the Board. If otherwise given, the director must take reasonable steps to see that it is read at the first meeting of the Board after the same is given. The sec. does not affect any provision of law restricting a director's interest or concern in a contract or arrangement with the Co. Notice that the effect of non-

(x) *Neal v. Quinn* (1916) W.N. 223.

(y) *Cambell's Case* (1876) 4 Ch.D. 470.

disclosure of his interest by a director in a contract with the Co. is that under s. 283, he automatically vacates his office as director.

(vii) Director not to vote on Contract in which interested: Under s. 300, a director who is directly or indirectly interested or concerned in any contract or arrangement with the Co. as above, is prohibited, as such director, from participating in any discussion about the same and/or from voting thereon. His presence shall not also count for the purpose of quorum, and if he votes, his vote shall be void. The sec. however does not apply to: (i) a private Co. (not being a subsidiary or holding Co. of a public Co.), (ii) to a private Co. which is a subsidiary of a public Co., with regard to contracts or arrangements entered or to be entered into by such private Co. with the holding Co., (iii) to a contract of indemnity for loss which may be suffered by any director or directors by standing surety for the Co., (iv) to a contract with a public Co. (or a private subsidiary thereof), in which the director being nominated thereto by the first Co., is interested to the extent of his qualification shares in that Co. as director thereof, (v) to contract with public Co.s (or private subsidiaries thereof), as regards which the Central Government in public interest has notified that the above provisions shall not apply with or without modifications. A director knowingly contravening the provisions of the sec. is punishable with fine. Though an interested director cannot vote as a director, it has been held that he can vote as a shareholder when the matter is put before the general meeting of the Co. (z).

Register of Contracts covered by ss. 297 and 299: Under s. 301, every Co. must keep a register of contracts or arrangements in which a director is interested and which are covered by ss. 297 and 299. The following particulars shall be entered therein: (i) date of contract or arrangement, (ii) names of parties thereto, (iii) principal terms and conditions thereof, (iv) date when it was placed before the Board, and (v) names of directors voting for and against it and of those who remained neutral. The above shall be entered in the register within 3 days of the meeting at which the same is approved. The register shall be placed before the next meeting of the Board and shall be signed by all directors present. It shall also specify, in connection with each director, the names of the firms and bodies corporate, with regard to which a general notice under s. 299(3) has been given. Penalty for default of any of the above provisions is a fine for the Co. and every officer in default. The register must be kept at the registered office of the Co. and shall be open for inspection of members (with power to make extracts and take copies), in the same way as the Register of members, and with the same conditions.

(viii) Disclosure to members where Director interested in appointment of Managing Agent, etc.: S. 302 provides that where a Co. enters into a contract for appointing a Manager, in which contract a director is directly or indirectly interested, or varies such contract, the Co. shall, within 21 days thereof, send to every member, an abstract of the terms or variation, with a memo., clearly specifying the interest or concern of the director therein. A similar procedure as regards sending the abstract is also to be followed by the Co., where the Co. enters into or varies a contract for the appointment of a managing director. Where a director is interested or concerned as above in any such appointment, a similar memo. has also to be sent to all the members as above.

Where a Co. proposes to enter into or vary any contract for appointment of managing agent or secretaries and treasurers, in which a director is interested or concerned, the abstract of the terms and the memo., showing the director's interest as above, shall be sent to all members in sufficient time before the general meeting wherein the proposal is to be considered. If a director becomes interested or concerned in any such contract or variation, after such meeting is held the abstract and memo.s mentioned above, shall be sent to all members within 21 days of such interest or concern arising. Penalty for default is a fine for the Co. and officer in default.

All contracts for the appointment of managing agent, managing director, manager, secretaries and treasurers, shall be kept at the Registered office of the Co. Inspection thereof (with right to extracts and copies), can be taken by members in the same

manner and subject to the same conditions as in case of the Register of members. The above provisions apply also to a resolution or proposed resolution of the Board, appointing manager, managing or whole-time director, or varying any previous contract or resolution with regard to the same.

Assignment of Office by Directors : Any assignment of his office by a director after the commencement of the Act shall be void (s. 312). The prohibition against assignment is now absolute.

Director, etc. not to hold Office of Place of Profit under Company : S. 314 provides that except with the previous sanction of a special resolution of the Co., no director or partner or "relative" of such director, no firm in which such director or "relative" is a partner, no private Co. of which such director is director or member and no director, managing agent, secretaries and treasurers or manager of such private Co., shall hold any "place" or "office of profit" under the Co. *except* that of managing director, managing agent, secretaries and treasurers, manager, legal or technical adviser, banker or trustee for debenture-holders. The same restrictions apply with regard to subsidiary of the Co. also, unless the remuneration received from such subsidiary is paid over to the Co. or its holding Co. A director contravening the above provisions shall be deemed to have automatically vacated his office from the first day of such contravention. He shall also be liable to refund all remuneration or other monetary equivalent received by him in connection with such office in the shape of perquisites or otherwise.

"Holding of office or place of profit" includes as regards director, receiving any remuneration in excess of remuneration receivable as director, whether the excess consists of a salary, fees, commission, perquisites, rent-free premises for residence or otherwise; in case of another individual, firm, private Co. or other body corporate, it includes obtaining anything by way of remuneration, whether as salary, fees, commission, perquisites, rent-free premises or otherwise.

The above provisions of the sec. have far-reaching effects. The prohibition against acceptance of office or place of profit under the Co. now extends to (i) a director, (ii) his partner, (iii) his "relative" as defined by s. 6, (iv) to a firm in which either the director or his "relative" is a partner, (v) to a private Co. of which the director is a director or member, and (vi) to a director, managing agent, secretaries and treasurers and manager of such private Co. as is mentioned in (v) above. All these parties accept or, after the Act comes into operation, continue in an "office" or "place of profit" under the Co. at their own peril and also at the peril of the director concerned who automatically vacates his office immediately the contravention occurs, i.e. if sanction of the Co. by means of a special resolution, confirming such appointments is not forthcoming as provided by the sec. The office or place of profit may be under the Co. or its subsidiary. A director obtaining remuneration otherwise than as a director, e.g. as salary, fees, commission, perquisites or rent-free accommodation or otherwise howsoever, is within the sec. In the other cases, e.g. in case of individual, firm, private Co. and body corporate, if they obtain anything by way of remuneration, whether as salary, fees, commission, perquisites, rent-free premises or otherwise howsoever, they also will be covered by the sec. Notice that holding office under the Co. as managing director, managing agent, secretaries and treasurers, manager, legal or technical adviser, banker or trustee for debenture-holders is not within the mischief of the sec., nor apparently, the holding of such offices in a subsidiary of the Co. In case of a subsidiary, it would further appear that an office or place of profit can be held therein by the prohibited persons, provided all remuneration received by them in respect thereof is paid over by them to the holding Co. The sec. makes all appointments contrary to its provisions bad. Notice that the sec. applies, not only to public Co.s but to private Co.s as well. The object is, of course, to prevent nepotism behind the back of shareholders.

Register of Directors : Every Co. must maintain at its Registered Office, a register of directors, managing director, managing agent, secretaries and treasurers, manager and secretary and enter therein: (i) in case of individual, his full name, surname, former full name or surname, with residential address, nationality (and nationality of origin, if changed later), business, occupation, and (except in case of private Co. which is not a subsidiary of a public Co.) the date of birth, and particulars of any office of director, managing director, managing agent, secretaries and treasurers, manager or secretary

held by him in any body corporate, (ii) in case of a body corporate, its corporate name, registered or principal office, full name and address and nationality (with nationality of origin if different), of each of its directors, and if it holds any office of managing agent, secretaries and treasurers, manager or secretary, in any other corporate body, particulars of each of the offices, (iii) in case of a firm, the same particulars as regards each of its partners, (iv) if any director or directors have been nominated by a body corporate, its corporate name and full particulars as stated in (i), in respect of each director so nominated and as regards the corporate body, all particulars mentioned in (ii) above, (v) if any director or directors have been nominated by a firm, full particulars as mentioned in (i) as regards each partner thereof and the same with regard to the firm as mentioned in (ii) above (s. 303). "Director", in the above connection, includes a person "in accordance with whose instructions the Board is accustomed to act". The Co. must, within 28 days of the appointment of first directors, send to the Registrar, in the prescribed form, a return containing the above particulars in the Register. Any change in directors, managing directors and the others and in the said particulars, shall also be notified to the Registrar, in the prescribed form, within 28 days of the change. Penalty for default is a fine for Co. and officer in default. The register shall be open to inspection of members without fee, subject to reasonable restrictions and to outsiders, on payment of Re. 1 for each inspection. Penalty for refusal is a fine for the Co. and officer in default. The Court may also direct immediate inspection (s. 304). The Registrar shall also keep a separate register or registers in which the particulars filed with him under s. 309 shall be entered (all returns with regard to each Co. being together). Inspection of the same can be taken by the public during office hours on payment of prescribed fee (s. 306). The person mentioned in s. 302 (including "the person on whose advice the Board is accustomed to act"), shall, within 28 days of their appointment as such, disclose to the Co. all particulars as regards their office in any other body corporate which are required to be specified under s. 303. Failure is punishable with fine (s. 305).

Register of Director's Shareholdings: Every Co. must also maintain a register showing, as regards each director (including therein "the person on whose advice the Board is accustomed to act") the number, description and amount of shares or debentures of the Co. or its subsidiary or holding Co. or subsidiary of the holding Co., which are held, (i) by him or (ii) in trust for him, or (iii) of which he has a right to be a holder, whether on payment or not. Where any shares or debentures have to be recorded in or omitted from such register, by reason of any transaction with regard to them after the commencement of the Act, the register shall show the date, the price or other consideration for the same. If there is an interval between the agreement and the completion of the transaction, the date of the agreement shall be shown. If the director requires, the nature and extent of the director's interest in the shares and debentures shall also be recorded therein. The register shall be kept at the Registered office and shall be open for inspection (subject to reasonable restrictions), during business hours by all members and debenture-holders from 14 days before, to 3 days after the conclusion of the annual general meeting (Saturdays, Sundays and holidays being excluded). It shall also be produced at the commencement of and shall be kept accessible to every member entitled to attend the meeting, during every annual general meeting. (Penalty for default as to the last, is a fine for the Co. and officer in default.) The Register shall be open to inspection of the Registrar or any person acting for the Central Government at any time. The Central Government or the Registrar may require a copy of the Register or part thereof to be furnished to them. The Co. shall not be fixed with notice of the right or interest of other persons with regard to the aforesaid shares and debentures by reason of the aforesaid recording. Default in maintaining the Register, in entering the required particulars therein, for failure to give inspection or copy within reasonable time, is punishable with fine (and a further fine per day till the default continues). A director shall be deemed to hold, have interest or right in or over any shares or debentures, if another corporate body holds them or has an interest in or right over them, and the body corporate or its Board is "accustomed to act according to his directions or instructions" or he is entitled to exercise or control the exercise of 1/3rd of the total voting powers of the same, at any general meeting thereof.

Under s. 308, persons abovementioned must give notice to the Co. of all necessary matters, to enable the latter to comply with the provisions of s. 306. The notice must

be in writing and shall be given at a Board meeting. If otherwise given, the person must take all reasonable steps to bring up and have the notice read at the Board Meeting held next after the notice is given. Penalty is a fine or imprisonment or both, for person failing to comply with above provisions.

Directors to carry on Business: The Board of directors can carry on or arrange for the carrying on of the affairs of the Co. where the managing agent or secretaries and treasurers thereof have vacated or have been suspended from their respective offices, or have ceased to act as such or where a permanent or temporary vacancy occurs with regard to them. They can do so till either the above parties again become entitled to act as such or the Co. in general meeting resolves otherwise (s. 298).

Directors with Unlimited Liability: If the Memo. so provides, the liability of a director, managing director, managing agent, secretaries and treasurers or manager of a limited Co. may be unlimited. Written notice of the aforesaid fact must be given to such persons before their appointment by either the promoters, directors, managing agents, secretaries and treasurers or manager of the Co., and a statement of the said fact shall also be added to the proposal for his appointment by any of the above persons or by the proposer. Default in adding the above statement or in giving the above notice is punishable with a fine for the above parties in default and they shall also be liable for any damage caused to the person thereby but the liability of the appointee shall not be affected thereby (s. 322). A limited Co. can, if authorised by the articles by special resolution, alter its Memo. so as to render the liability of any of the above persons unlimited. On such amendment, alteration shall be deemed to be part of the Memo. from the beginning, but the liability of the person shall not be altered thereby until the expiry of his then term of office, unless consented to by him (s. 323). *For Remuneration of Directors and Compensation for loss of Office, see seq.*

Validation of Acts of Directors: Acts done by a person as director shall be valid, notwithstanding that his appointment is afterwards discovered to be invalid by reason of defect or disqualification or by reason of its termination under the Act or articles. No such act however shall be valid if done after the director's appointment is shown to be invalid to the Co. (s. 290). The sec. has the effect of making the acts of *de facto* directors as good as those of *de jure* directors, if the former have acted honestly (a). The sec. cures defect in the appointment of directors or qualification of directors. But where there is no appointment of a director at all, but there has been a fraudulent usurpation of authority by him, the sec. will not apply (b). The sec. cannot validate acts of a director whose appointment is defective, if the other party was aware of the defect or was put upon an inquiry in that behalf by the circumstances of the case but failed to make such inquiries. In the latter case, it is no defence to say that if such inquiry had been made in fact, the person would have obtained false answers (c).

Directors and Outsiders

Persons dealing with directors will be presumed to have notice of the instrument conferring authority on them, e.g. the Memo. and the articles of the Co. That is the reason why these documents are required by law to be registered with the Registrar of Companies. The Memo. and articles in fact, are public documents and they have been held to be such, as pointed out before. Persons dealing with Co.s, therefore, are bound to inquire into (and if they fail to inquire, will be fixed with notice of) the contents of the articles and Memo. of the Co. Any action of the director of a Co., therefore, which is contrary to the provisions of the Memo. or articles of the Co., will not, generally, be binding on the Co., even though the outsider dealing with the director was, in fact, unaware of the same. Outsiders, however, are not bound to inquire and will not therefore be presumed to know, whether all the regulations of the Co., relating to its internal management and the conduct of its business, have been duly and properly complied with or not. In other words, they will not be fixed with notice of matters which relate to what has been called "*the indoor management of the Co.*" and they

(a) British Asbestos Co. v. Boyd (1903)
2 Ch. 439.

(b) Morris v. Kanssen (1946) A.C. 459.
(c) Kanssen v. Rialto Ltd. (1944) Ch. 346.

will not be affected by any irregularities that may take place or have taken place therein. This is called the "*Rule in Royal British Bank v. Turquand* (d).

There are, however, certain exceptions to the rule: (i) The rule does not extend to cases where outsiders have in fact notice of the irregularity, even though such irregularity relates to matters of "indoor management" of the Co. Thus where debentures were issued in favour of I, a director, which were in excess of the borrowing powers of the directors and at the meeting of directors at which the issue was sanctioned, I was present, it was held that the debentures were invalid, I, having notice of the defect in their issue (e). On the same principle, if directors enter into a fraudulent arrangement or agreement with another, it will not be binding on the Co., if the other party was actually a party to the fraud.

(ii) The doctrine that an outsider need not investigate whether or not the conditions regulating the internal management of the Co. have been strictly carried out, in accordance with the articles, has no application to the case of a document which is an obvious forgery. The Co., in such a case, will not be precluded from denying the authority of the person who purports to sign the document, and from repudiating all liability in respect of the same. The above rule cannot be relied upon in such cases. Thus in *Ruben v. Great Fingall Consolidated* (f), the seal of the Co. was affixed by the secretary to a share certificate, without the authority of the Co. He had also forged the signature of two directors thereon. Held, the document was a forgery and the Co. was not bound thereby. The rules, such as can be laid down from the decided cases on this point, appear to be these: (a) if the Co. has only a limited power to do an act, e.g. to borrow upto a certain limit, the person who lends will be affected with the limitation (g). (b) If articles give power to an officer to do certain act, provided certain directions are observed, the person dealing with the Co. is entitled to assume that the officer doing the act, followed the directions. (c) If the articles merely empower the directors to delegate their powers, then if the act is one which would ordinarily be beyond the power of the officer, the person dealing with the Co. cannot assume that directors have, in fact, delegated the power (h). (d) If the act is ordinarily within the power of the officer, the Co. cannot dispute the authority of the officer to do that, whether actual delegation has taken place or not (i). (e) An act, which in effect, amounts to a forgery, will not bind the Co., no question of supposed authority arises in such a case (j). (f) Lastly, even if wide powers of delegation are given to the directors by the articles, still, if the third party was in fact ignorant of these powers and acted without relying on them, the Co. will not be bound.

(iii) Notice that though a person dealing with a Co., has notice that a particular act is not properly authorised, still, if the Co. derives a benefit from the act, it will be required to pay for the same. Thus where plaintiff was appointed managing director of a Co. by an agreement under the seal of the Co. which provided for his remuneration, but the directors had not passed any resolution, nor had they obtained their qualification shares, and the plaintiff was aware of these defects, it was held that though the agreement was void, the plaintiff was entitled to recover on "quantum meruit" (k).

Duties of Directors

Directors are bound to comply with the provisions of the Companies Act and to carry out generally all duties placed upon them by either the Act or the articles. As regards the duties of directors with respect to the general administration of the Co.'s affairs, they were considered in detail and laid down by Romer J. (as he then was), in *Re City Equitable Fire Insurance Co.'s Case* (l) as follows:

"In order to consider the duties that a person appointed to the Board of an established Co. undertakes to perform, it is necessary to consider not only the nature of the

(d) (1856) 6 E. & B. 327.

(e) *Howard v. Patent Ivory Co.* (1888) 38 Ch.D. 156.

(f) (1906) A.C. 439.

(g) *Fountain v. Carmarthen Rly. Co.* (1868) L.R. 5 Eq. 316.

(h) *Haughton & Co. v. Natherd Law & Wells* (1928) A.C. 1.

(i) *Day v. Pullinger.*

(j) *Kredit Bank's Case* (1927) 1 K.B. 826.

(k) *Craven Ellis v. Cannon* (1936) 2 K.B. 403.

(l) *Supra.*

Co.'s business but also the manner in which the work of the Co. is in fact distributed between the directors and other officers of the Co., provided this distribution is always a reasonable one in the circumstances and is not inconsistent with any express provisions of the articles of association. In discharging the duties of his position, thus ascertained, a director must, of course, act honestly but he must also exercise some degree of both skill and diligence. To the question, what is the particular degree of skill or diligence required of him, the authorities do not, I think, give any very clear answer. It has been laid down that so long as a director acts honestly, he cannot be made responsible in damages, unless guilty of gross or culpable negligence in a business sense. But as pointed out by Nevill J. in *Re Brazilian Rubber Plantation Estate Ltd. (m)*, one cannot say a man has been guilty of negligence, gross or otherwise, unless one can determine what is the extent of the duty which he is alleged to have neglected. For myself, I confess to feeling some difficulty in understanding the difference between negligence and gross negligence, except in so far as the expressions are used for the purpose of a distinction between the duty that is owed in one case and the duty that is owed in the other. If two men own the same duty to a third person and neglect to perform that duty, they are both guilty of negligence and it is not altogether easy to understand how one can be guilty of gross negligence and the other of negligence only. But if it is said that of two men, one is only liable to the third person for gross negligence and the other is liable for mere negligence, this, I think, means no more than that the duties of the two men are different. The one owes a duty to take a greater amount of care than does the other. See the observations of Wills J. in *Grill v. General Iron Screen Collier Co.* If therefore a director is only liable for gross or culpable negligence, this means that he does not owe a duty to his Co. to take all possible care. It is some degree of care less than that. The care he is bound to take has been described by Nevill J., in the case referred to above as "reasonable care", to be measured by the care an ordinary man may be expected to take in the circumstances on his own behalf. In saying this, Nevill J. was only following what was laid down in *Overend Gurney Co. v. Gibb (n)*, as being the proper test to apply, viz. "whether or not, the directors exceeded their powers entrusted to them or whether if they did not so exceed their powers, they were cognisant of circumstances, of such a character, so plain, so manifest and so simple of appreciation that no man with ordinary degree of prudence acting on his own behalf, would have entered into such a transaction as they entered into."

"There are in addition, one or two other general propositions that seem to be warranted by the decided cases: (i) A director need not exhibit in the performance of his duties a greater degree of skill than may reasonably be expected from a person of his knowledge and experience. A director of a life insurance Co. for instance, does not guarantee that he has the skill of an actuary or of a physician. In the words of Lindley M.R.: "if directors act within their powers, if they act with such care as is to be reasonably expected of them having regard to their knowledge and experience and if they act honestly for the benefit of the Co. they represent, they discharge both their equitable as well as legal duty to the Co. (o). It is perhaps only another way of stating the same proposition to say that directors are not liable for mere errors of judgment. (ii) A director is not bound to give continuous attention to the affairs of the Co. His duties are of an intermittent nature to be performed at periodical Board meetings and at meetings of any committee of the Board upon which he happens to be placed. He is not bound, however, to attend all such meetings, though he ought to attend wherever in the circumstances he is reasonably able to do so. (iii) In respect of all duties that, having regard to the exigencies of business or the articles of association, may properly be left to some other official, a director is, in absence of any grounds for suspicion, justified in trusting that official to perform such duties honestly."

Liability of Directors

The liability of directors has to be considered from various points of view: (i) Directors may become liable to the shareholders in a variety of ways. (ii) Directors may also become liable to outsiders in certain cases. The liability may be civil and/or criminal.

(m) (1911) 1 Ch. 425.
(n) (1872) 5 H.L. 480.

(o) *Luganos Nitrate Co. v. Luganos Syndicate* (1899) 2 Ch. 392.

Liability to Outsiders: As regards contracts entered into by directors on behalf of the Co., the directors cannot generally be made personally liable therefor. This is because they act as agents of the Co. (p). They may become personally liable, however, where they act without the authority of the Co., as on a breach of warranty of authority (q). They may also become personally liable on contracts entered into on behalf of the Co., when by words used or by necessary implication, they have personally undertaken to be responsible for the same (r).

As regards torts, a director who himself commits or authorises a tortuous act is personally liable therefor and this also if he is acting as agent of the Co. Similarly, a director is personally liable for any fraud committed or authorised by himself, e.g. issue of a fraudulent prospectus. A director however is not liable for the fraud of his co-director, unless it is authorised by him or he has participated therein (s).

As regards wrongs committed by the Co. to outsiders, directors are not liable for the same, unless (i) the directors authorised the wrong or the Co. was the agent of the directors to do the wrong. It has been held by the Privy Council that a Corporation cannot be held incapable of malice so as to be relieved of liability for malicious libel when published by its servant in the course of his employment. Although a servant may not have actual authority, express or implied, to write the libel complained of, containing statements against the person libelled which he knew to be untrue, if he did so in the course of his employment which was authorised, the corporation is liable (t).

Liability to Shareholders: Directors may become liable to the shareholders of the Co. in a variety of ways. They may become liable for (i) negligence, (ii) for misfeasance, and (iii) for breach of trust. (iv) They may also become liable by virtue of statutory liability placed upon them in certain cases.

Liability for negligence: Where directors acting within their powers fail to use such reasonable skill and diligence as may be expected from persons with their knowledge and experience in the management of the Co.'s affairs, they can be held liable for negligence (u). They are not liable for errors of judgment causing loss to the Co., provided they acted *bona fide* for the benefit of the Co. and with such care as may be reasonably expected from them (v). The burden of proving bad faith in such a case is on the person challenging the act of the directors (w). Where a discretion is left to the directors to do or not to do a particular act, honest, though imprudent, exercise of the same will not make directors responsible for negligence in respect of "ultra vires" act.

Directors are not justified in blindly leaving everything to managing agents. Thus in a Bombay case (x), the defendant was one of the five directors of a bank which subsequently went into liquidation. The business of the bank was managed by the other four directors, who were also the secretaries, treasurers and agents of the bank. The agents opened a branch in Bombay without any resolution of the Board in that behalf. They also advanced moneys to bogus Co.s. in one of which one of them was personally interested. They also advanced loans to various persons without specific security and also to themselves in various indirect ways. They also allowed claims of the Bank against customers, some of them their own friends to be time-barred. No rules for guidance of agents in making loans were framed by the directors. No balance sheets were issued for 3 years and such as were issued were false, showing exaggerated amount of debts as secured, when they were not so, and showing other debts as good debts, when they were in fact not so. For a series of years, there had been only two effective meetings of directors per year. *Held*, that the defendant, though he did not

(p) *Fergusson v. Wilson* (1866) L.R. 2 Ch. App. 77.

(q) *Collen v. Wright* (1957) 7 E. & B. 301; *Coventry's Case* (1891) 1 Ch. 202.

(r) *Dermatine v. Ashworth* (1905) 21 T.L.R. 510.

(s) *Prefontain v. Granier* (1907) A.C. 101.

(t) *Citizen Life Ass. Co. v. Brown* (1904) 2 Ch. 423.

(u) *Re Equitable City Fire Ins. Co.* (1925) Ch. 407.

(v) *Luganos Nitrate Co. v. Luganos Nitrate Syndicate* (supra)

(w) *Re Liverpool Household Stores* (1890) 59 L.J.Ch. 616.

(x) *Govind v. Raghunath*, 32 Bom. L.R. 232.

actually participate in the fraud of the other directors, was guilty of negligence in blindly leaving everything relating to the Co.'s affairs in the hands of his co-directors, who were the actual authors of the fraud.

Liability for Misfeasance and Breach of Trust: These are two allied heads of liability: "Misfeasance" being defined as any breach of duty in the conduct of the Co.'s affairs which causes loss to the Co., "breach of trust" being confined to any misapplication of the funds of the Co. Thus paying dividend out of capital (y), or using the funds of the Co. for ultra vires purposes (z), is a breach of trust. To allot shares to an infant (a), to give a fraudulent preference to a creditor or to commit any breach of the articles, would be misfeasance. If directors misuse their powers as directors for their own advantage, the transaction as against the Co. is of no effect and the Court will not inquire whether the Co. derived any benefit from the transaction (b).

Liability for "Ultra Vires" Acts: Where directors do any act which is in excess of their powers, e.g. borrow money or create a mortgage which is beyond their authority as defined by the articles, such act is called "ultra vires" the directors. If, however, it is not beyond the powers of the Co. as laid down by the Memo., the shareholders can, by subsequent ratification, make the act, which is "ultra vires" the directors but "intra vires" the Co., valid and binding on the Co. (c). In order to prove ratification, however, two points must be established: (a) that the shareholders who ratified had full and clear knowledge of the act and (b) that all the shareholders ratified and not merely those who were present at the meeting. The ratification can be by a formal resolution at an ordinary general meeting or at an informal meeting of the shareholders. It may also be inferred from acquiescence (d). To render valid an act of the directors which is "ultra vires", the acquiescence of the shareholders must be of the same extent as the consent which would have given validity from the first, viz. the acquiescence of each and every member. This acquiescence cannot be presumed, unless knowledge of the transaction can be brought home to every one of the shareholders. By knowledge of the transaction is clearly meant the knowledge of the invalidity of the transaction. There can be no ratification without an intention to ratify and there can be no intention to ratify an illegal act without knowledge of its illegality (e).

Even where there has been no such ratification, it does not follow that contractual rights which have arisen from the "ultra vires" acts of the directors, cannot be enforced against the Co. Thus though a borrowing may be "ultra vires" the directors, still if it is "intra vires" the Co., the moneys can be recovered from the Co. in an action for money had and received (f). The directors, however, cannot do anything which is beyond the instrument constituting the Co., i.e. the Memorandum. Thus where a clause in the Memo. of a public Co. empowered the directors to grant pensions to the employees of the Co. or to their wives and children, it was held that this did not justify the directors in granting an annual pension to the widow of a pre-deceased director. It was further held that the fact that the shareholders have individually assented to such payment, will not make it binding on the liquidator (g).

Criminal Liability of Directors: As to criminal responsibility under the Act, see sec. 115 (keeping register of members), s. 162 (annual list and summary), s. 95 (notice to Registrar as to conversion of shares and stocks), s. 168 (calling general meeting), s. 192 (sending copies to Registrar of special resolutions), s. 303 (keeping register of directors), s. 75 (proper return of allotment), s. 113 (keeping certificates ready for delivery), s. 143 (keeping register of mortgages and charges and allowing inspection thereof) and other secs. of the Act, which lay down particular penalties for breach of various duties of directors under the Act. Ss. 627-631 lay down further provisions for prosecution of directors, e.g. for preparing false reports, returns, certificates and balance

(y) *Flitcroft's Case* (1882) 21 Ch.D. 579.

(z) *Cullern v. London etc. Society* (1890) 25 Q.B.D. 485.

(a) *Ex parte Wilson* (1878) 8 Ch.App. 45.

(b) *E.B.M. Co. v. Dominion Bank, A.I.R.* (1937) P.C. 729.

(c) *London Financial Asso. v. Kelk* (1884) 26 Ch.D. 107.

(d) *Parkar v. Reading* (1936) 1 Ch. 975.

(e) *Pramila Devi v. People's Bank of N. India, A.I.R.* (1938) P.C. 284.

(f) *Pratt (Bom.) Ltd. v. Sassoon Ltd.*, 37 Bom. L.R. 978.

(g) *Re Lee Bahrans & Co. Ltd.* (1932) 2 Ch. 46.

sheets, for wrongfully withholding property of the Co. and for employing the funds of the employees of the Co. for improper purposes. Ss. 538-545 lay down further provisions for penalty for falsification of books, prosecution of delinquent directors, for penalty for giving false evidence, and for not discovering the Co.'s property or not handing over the Co.'s documents.

Statutory Protection to Directors: S. 633 of the Act provides statutory protection to directors and others who have been in default, if the Court, under the circumstances of any particular case, feels that the particular director or officer should be excused. The sec. provides that if in any proceedings for negligence, default or breach of trust against any officer of the Co., it appears to the Court trying the proceedings that such person is or may be liable for the same, but that he has acted honestly and reasonably and that having regard to all the circumstances of the case, including those connected with his employment, he ought to be fairly excused, the Court may relieve him partly or wholly from liability for the same on such terms as the Court thinks fit.

The sec. gives further power to an officer of the Co. who has reason to apprehend that any claim will or might be made against him for any of the aforementioned acts or neglects, to apply to the Court for relief and on any such application, the Court shall have the same power to relieve him, as if it was a Court in which proceedings against the Officer under the first cl. were pending.

Extra Protection to Directors: Though the directors are at law liable to the Co. in the manner stated above, articles of Co.s very often used to contain provisions exempting them from liability, either absolutely or to a limited extent. These clauses were called "indemnity clauses" and they usually ran in some such form, viz. "the director shall not be answerable, otherwise than in respect of his own acts or defaults nor shall be liable for any loss or damage happening to the Co. by anything done by him in execution of his office or by reason of any error of judgment or mere indiscretion in the execution of his duties or otherwise on any account whatsoever, except only through his wilful default or neglect".

Where such indemnity clauses existed in the articles, they often used to afford complete protection to the directors against all acts or defaults on their part, however great the loss they may cause to the Co. and however grossly negligent they may themselves have been in the commission of the said acts or defaults.

In order to prevent this abuse of power in framing articles, s. 201 provides that save as provided therein, provisions contained in the articles or in any agreement with the Co. or in any other instrument, exempting any officer of the Co. or any person employed as an auditor of the Co. from any liability or indemnifying him against any liability which by virtue of any law would otherwise attach to him in respect of negligence, default, misfeasance, breach of duty or breach of trust in relation to the Co. shall be void. The Co. may however in pursuance of any such provision, indemnify such officer or auditor against costs incurred in defending proceedings, civil or criminal, taken against him in the above respects, provided they have ended in his favour or if he has been discharged or acquitted in respect thereof. Costs of application for relief, made by him under s. 633, if successful, may also be indemnified against, by the Co. The above privileges however are not to be available to a constituted attorney of managing agent, unless he falls within the definition of "officer" under s. 2 of the Act.

Remedies against Directors: While the Co. is a going concern, the remedy of the Co. against a delinquent director is by way of action in the Civil Court. If the Co. is being wound up, a summary remedy is provided for this purpose in the shape of a "misfeasance summons" under s. 543 of the Act. A right of action however is not barred. (For misfeasance summons see seq.)

Directors and Investment of Company's Funds: An improvement of major importance has been the introduction of detailed provisions in the present Act as regards the investment of the funds of a Co. This is a subject of vital importance in Co. management, as often, the success or failure of a Co.'s life may depend on the safe and well regulated investment of its funds by those in charge of its administration.

Under s. 49, all investments made by a Co., on its own behalf, shall be made and held by it in its own name. Where at the time of commencement of the Act, such investments are held otherwise than as above, the Co. shall, within one year thereafter, have the same transferred to its own name or dispose them off. The above rule is subject to the following exceptions: (a) where a Co. has power to appoint directors of another body corporate, shares in the latter, equal to the necessary qualifications, may be held by the Co., either in its own name jointly with its nominee or nominees, or in the name of the nominee or nominees, expressly described as such nominee or nominees. (b) A Co. may hold shares in the name of its nominee or nominees in any subsidiary of the Co., to an extent sufficient to secure that the number of members of such subsidiary is not reduced below 7 in case of public and below 2 in case of a private Co. (c) A Co. may deposit shares and securities belonging to itself with its bankers as such for the collection of interest or dividend. (d) A Co. may deposit or transfer to any person, shares or securities belonging to it, as security for repayment of a loan or the performance of an obligation. (e) Where a Co.'s principal business consists of buying and selling shares and securities, such Co. is free to hold its shares and securities in names other than its own. In cases falling under the operative part of s. 49 and in case of exception (a) the certificates of shares or securities (or the letters of allotment with reference to the same), in which the investments have been made, shall be kept in the custody of the Co., or with a scheduled Bank, being the bankers of the Co. In case of exceptions (b), (c), (d) and (e), the Co. shall enter all such shares and securities in a separate register to be maintained for the purpose showing the nature, value and all other particulars necessary to identify the same, together with the name of the person or bank in whose name or custody the shares and securities are held. Such register shall be open for inspection to any member or debenture-holder of the Co. free of charge, during business hours, subject to reasonable restrictions. Default in complying with the above provisions is punishable with a fine upto Rs. 5,000 for the Co. and every officer in default. The above provisions apply to all Co.s, public as well as private.

MANAGING AGENTS AND THEIR "ASSOCIATES"

Abolishing Managing Agents by Notification: S. 324 provides that subject to rules as may be prescribed, the Central Government may, by Notification in the Official Gazette, declare that from a specified date with regard to all Co.s (whether incorporated before or after the commencement of the Act), which are engaged or may thereafter engage, whether wholly or in part, in specified class or description of industry or business, the term of office of their managing agent shall be determined (if not determined earlier), at the end of 3 years from the specified date or on 15th August 1960, whichever is later and where such Co. has no managing agent, or where it is incorporated on or after that date, that it shall have no managing agent at all.

In the present Act, opportunity is taken to reconsider the entire question of the appointment and the limitations of the powers of managing agents and by ss. 324-376, suitable regulations have been framed for preventing them from abusing their powers and authority.

Copies of all rules made under cl. (1) of the sec. shall, as soon as they have been prescribed, be laid before both Houses of Parliament. A copy of every Notification proposed to be issued under the sec., must be laid in draft before both Houses of Parliament for not less than 30 days when the Houses are in Session, and if within that period either House disapproves of the Notification or approves the same with modifications, such Notification shall not be issued or issued with modifications agreed upon by both Houses. The exercise of the above drastic powers of abolishing the whole system of managing agency conferred by the sec. on the Central Government is subject to two limitations: (i) it can be exercised only subject to the previous sanction of both Houses of Parliament. It cannot be exercised as and by way of an executive fiat; (ii) it can be exercised not with regard to an individual Co. or business or industry but only with regard to all Co.s carrying on a particular class of business or industry. Where such notification is issued by the Central Government, existing managing agencies with regard to such Co.s will cease to function after 3 years from the date specified in the Notification or on 15th August 1960 whichever is later.

S. 325 provides (i) that after the commencement of the Act, no managing agency Co. shall appoint managing agent for itself, whatever its business may be. Further, no Co. having a managing agent, shall act as the managing agent of another Co. Appointments in contravention of the above are void. (ii) Where at the commencement of the Act a Co. having a managing agent, is itself managing agent of another Co., the term of agency of the former Co. shall expire on 15th August 1956 (if it has not expired earlier under the provisions of Act of 1913 or other relevant enactments).

Appointment and Term of Office of Managing Agent

As regards Co.s to which none of the provisions of ss. 324 and 325 mentioned above apply, s. 326 provides that in such Co.s, a managing agent shall not be appointed or "reappointed" except (i) by the Co. in general meeting and (ii) unless the appointment or "reappointment" is approved by the Central Government. The Central Government shall not grant its approval unless (i) it is satisfied that it is not against the public interest to allow the Co. to have a managing agent, (ii) that the proposed managing agent is a fit and proper person, and that the conditions of the proposed managing agency agreement are fair and reasonable, and (iii) that the managing agent has fulfilled any conditions required by the Central Government.

Under s. 328, (i) after the commencement of the Act, no Co. appointing a managing agent, for the first time, shall appoint him for more than 15 years, (ii) in other cases, appoint or "reappoint" managing agent for more than 10 years at a time, and (iii) "reappoint" a managing agent for a fresh term, any time before 2 years of his current term remain unexpired. The Central Government may, however, if satisfied that in the interest of the Co. it is necessary to do so, sanction the "reappointment" earlier. "Reappointment" does not include reappointment of a person on fresh, additional or changed conditions for the remaining unexpired period of his term but otherwise includes renewal or extension of the term of previous appointment and the appointment of another person having interest in the previous managing agency agreement. Contravention of the above will make the whole appointment or "reappointment" void (s. 328). Under the sec. "reappointment" does not include reappointment with changed terms, during the period of the original appointment, but if a new party is joined during the period, it would be "reappointment".

As regards persons holding office of managing agent at the commencement of the present Act, and who, therefore, till then, were governed by the provisions of the Act of 1913, s. 330 of the present Act provides that their term of office shall automatically expire on 15th August 1960 (unless before that date they are reappointed to the office, as provided by the Act as above). This is, of course, if their appointments have not been terminated earlier under the provisions of the Act of 1913 and its amending Acts. The result is that all managing agencies existing at the commencement of the present Act will terminate on 15th August 1960. If reappointment is desired, the necessary steps must be taken for the purpose between 15th August 1958 and 15th August 1960. This is because under s. 331, all provisions of the Act, excepting those relating to the term for which office of managing agent can be held, apply to every managing agent holding office at the commencement of the Act. Notice that the above provisions apply to private non-subsidiary Co.s also, unless specially exempted by Notification of the Central Government under s. 327.

Disqualified Managing Agent: An undischarged insolvent cannot act or discharge the functions of a managing agent nor can he directly or indirectly take any part or be concerned in the promotion, formation or management of the Co. Penalty for contravention of the above is imprisonment or a fine or both (s. 202). Further, where a person is convicted of an offence in connection *inter alia* with the management of the Co. or if in the course of winding up, it appears to the Court, that a person has been guilty of an offence punishable under s. 542 (fraudulent conduct of business) or has been otherwise guilty, while an officer of the Co., of any fraud, misfeasance, breach of duty or breach of trust in relation to the Co., the Court may make an order that such person shall not, without the leave of the Court, in any way, directly or indirectly, be concerned with or take part, *inter alia*, in the management of the Co. for a period not exceeding 5 years as the Court directs. Contravention of the above is punishable with imprisonment or fine or both (s. 203).

Under s. 49, all investments made by a Co., on its own behalf, shall be made and held by it in its own name. Where at the time of commencement of the Act, such investments are held otherwise than as above, the Co. shall, within one year thereafter, have the same transferred to its own name or dispose them off. The above rule is subject to the following exceptions: (a) where a Co. has power to appoint directors of another body corporate, shares in the latter, equal to the necessary qualifications, may be held by the Co., either in its own name jointly with its nominee or nominees, or in the name of the nominee or nominees, expressly described as such nominee or nominees. (b) A Co. may hold shares in the name of its nominee or nominees in any subsidiary of the Co., to an extent sufficient to secure that the number of members of such subsidiary is not reduced below 7 in case of public and below 2 in case of a private Co. (c) A Co. may deposit shares and securities belonging to itself with its bankers as such for the collection of interest or dividend. (d) A Co. may deposit or transfer to any person, shares or securities belonging to it, as security for repayment of a loan or the performance of an obligation. (e) Where a Co.'s principal business consists of buying and selling shares and securities, such Co. is free to hold its shares and securities in names other than its own. In cases falling under the operative part of s. 49 and in case of exception (a) the certificates of shares or securities (or the letters of allotment with reference to the same), in which the investments have been made, shall be kept in the custody of the Co., or with a scheduled Bank, being the bankers of the Co. In case of exceptions (b), (c), (d) and (e), the Co. shall enter all such shares and securities in a separate register to be maintained for the purpose showing the nature, value and all other particulars necessary to identify the same, together with the name of the person or bank in whose name or custody the shares and securities are held. Such register shall be open for inspection to any member or debenture-holder of the Co. free of charge, during business hours, subject to reasonable restrictions. Default in complying with the above provisions is punishable with a fine upto Rs. 5,000 for the Co. and every officer in default. The above provisions apply to all Co.s, public as well as private.

MANAGING AGENTS AND THEIR "ASSOCIATES"

Abolishing Managing Agents by Notification: S. 324 provides that subject to rules as may be prescribed, the Central Government may, by Notification in the Official Gazette, declare that from a specified date with regard to all Co.s (whether incorporated before or after the commencement of the Act), which are engaged or may thereafter engage, whether wholly or in part, in specified class or description of industry or business, the term of office of their managing agent shall be determined (if not determined earlier), at the end of 3 years from the specified date or on 15th August 1960, whichever is later and where such Co. has no managing agent, or where it is incorporated on or after that date, that it shall have no managing agent at all.

In the present Act, opportunity is taken to reconsider the entire question of the appointment and the limitations of the powers of managing agents and by ss. 324-376, suitable regulations have been framed for preventing them from abusing their powers and authority.

Copies of all rules made under cl. (1) of the sec. shall, as soon as they have been prescribed, be laid before both Houses of Parliament. A copy of every Notification proposed to be issued under the sec., must be laid in draft before both Houses of Parliament for not less than 30 days when the Houses are in Session, and if within that period either House disapproves of the Notification or approves the same with modifications, such Notification shall not be issued or issued with modifications agreed upon by both Houses. The exercise of the above drastic powers of abolishing the whole system of managing agency conferred by the sec. on the Central Government is subject to two limitations: (i) it can be exercised only subject to the previous sanction of both Houses of Parliament. It cannot be exercised as and by way of an executive fiat; (ii) it can be exercised not with regard to an individual Co. or business or industry but only with regard to all Co.s carrying on a particular class of business or industry. Where such notification is issued by the Central Government, existing managing agencies with regard to such Co.s will cease to function after 3 years from the date specified in the Notification or on 15th August 1960 whichever is later.

S. 325 provides (i) that after the commencement of the Act, no managing agency Co. shall appoint managing agent for itself, whatever its business may be. Further, no Co. having a managing agent, shall act as the managing agent of another Co. Appointments in contravention of the above are void. (ii) Where at the commencement of the Act a Co. having a managing agent, is itself managing agent of another Co., the term of agency of the former Co. shall expire on 15th August 1956 (if it has not expired earlier under the provisions of Act of 1913 or other relevant enactments).

Appointment and Term of Office of Managing Agent

As regards Co.s to which none of the provisions of ss. 324 and 325 mentioned above apply, s. 326 provides that in such Co.s, a managing agent shall not be appointed or "reappointed" except (i) by the Co. in general meeting and (ii) unless the appointment or "reappointment" is approved by the Central Government. The Central Government shall not grant its approval unless (i) it is satisfied that it is not against the public interest to allow the Co. to have a managing agent, (ii) that the proposed managing agent is a fit and proper person, and that the conditions of the proposed managing agency agreement are fair and reasonable, and (iii) that the managing agent has fulfilled any conditions required by the Central Government.

Under s. 328, (i) after the commencement of the Act, no Co. appointing a managing agent, for the first time, shall appoint him for more than 15 years, (ii) in other cases, appoint or "reappoint" managing agent for more than 10 years at a time, and (iii) "reappoint" a managing agent for a fresh term, any time before 2 years of his current term remain unexpired. The Central Government may, however, if satisfied that in the interest of the Co. it is necessary to do so, sanction the "reappointment" earlier. "Re-appointment" does not include reappointment of a person on fresh, additional or changed conditions for the remaining unexpired period of his term but otherwise includes renewal or extension of the term of previous appointment and the appointment of another person having interest in the previous managing agency agreement. Contravention of the above will make the whole appointment or "reappointment" void (s. 328). Under the sec. "reappointment" does not include reappointment with changed terms, during the period of the original appointment, but if a new party is joined during the period, it would be "reappointment".

As regards persons holding office of managing agent at the commencement of the present Act, and who, therefore, till then, were governed by the provisions of the Act of 1913, s. 330 of the present Act provides that their term of office shall automatically expire on 15th August 1960 (unless before that date they are reappointed to the office, as provided by the Act as above). This is, of course, if their appointments have not been terminated earlier under the provisions of the Act of 1913 and its amending Acts. The result is that all managing agencies existing at the commencement of the present Act will terminate on 15th August 1960. If reappointment is desired, the necessary steps must be taken for the purpose between 15th August 1958 and 15th August 1960. This is because under s. 331, all provisions of the Act, excepting those relating to the term for which office of managing agent can be held, apply to every managing agent holding office at the commencement of the Act. Notice that the above provisions apply to private non-subsidiary Co.s also, unless specially exempted by Notification of the Central Government under s. 327.

Disqualified Managing Agent: An undischarged insolvent cannot act or discharge the functions of a managing agent nor can he directly or indirectly take any part or be concerned in the promotion, formation or management of the Co. Penalty for contravention of the above is imprisonment or a fine or both (s. 202). Further, where a person is convicted of an offence in connection *inter alia* with the management of the Co. or if in the course of winding up, it appears to the Court, that a person has been guilty of an offence punishable under s. 542 (fraudulent conduct of business) or has been otherwise guilty, while an officer of the Co., of any fraud, misfeasance, breach of duty or breach of trust in relation to the Co., the Court may make an order that such person shall not, without the leave of the Court, in any way, directly or indirectly, be concerned with or take part, *inter alia*, in the management of the Co. for a period not exceeding 5 years as the Court directs. Contravention of the above is punishable with imprisonment or fine or both (s. 203).

An agreement by which the managing agent of a textile mill agrees to let in other persons into the management, jointly with himself, cannot be specifically enforced in view of the confidential relations subsisting between the mill Co. and the managing agents, as also the confidential relation with the co-agents themselves (h).

Declaration to be filed by Managing Agents: Every firm or private Co. which acts as managing agents of another Co. (public or private), and also every other body corporate (not being a private Co.), which acts as above, must file with the managed Co. a declaration as provided by Sch. VIII, giving the following particulars: (i) if the managing agents are a firm, the names of the partners at the "relevant date", the share or interest of each partner therein at such date, and the names of persons, other than partners, who at the said date, are entitled to share or have interest in the remuneration payable to the firm, for acting as managing agent, along with the nature and extent thereof. The declaration must be signed by a partner and must be filed with the Co. within one month of the "relevant date". Changes occurring in the above, must be similarly declared and filed with the Co. within 3 months thereof. (ii) *If the managing agents are a private Co.* the declaration must state the names of its members at the "relevant date", the shares held by each or the interest of each (if the Co. has no share capital) at such date, whether the shares or interest are held beneficially by such member or in trust for another and in the latter case, the name and nature and extent of such other therein; the names of the directors and managing director and the names of persons interested in any share in, or in the amount of remuneration payable to such private Co. by the other, otherwise than as members thereof, and the extent of such interest; and lastly, that no arrangement has been entered into by which the control of the private Co. is vested in persons other than its members and/or the real beneficial owners under the latter. The declaration must be signed by a director and must be filed within 2 months of the "relevant date". If to the knowledge of the private Co. a change occurs in any of the above matters or if an agreement for sale or transfer of any shares of the Co. is entered into or a sale or transfer thereof has taken place, such sale, transfer, agreement or change must be similarly declared and filed with the Co. within 6 weeks thereof. In such cases, the name of the person who parts with the shares, and the person who acquires them, must be also stated with full details of the sale transfer or agreement (s. 347).

If the managing agent is a body corporate (not being a private Co.), the same rules will apply, as in case of private Co. A body corporate whose shares are dealt with on a recognised stock exchange shall be exempted from the above requirements, unless the Central Government, by notification, otherwise directs. The exemption may be cancelled or modified also by the same authority.

Where more than one Co. are concerned, the above declarations are to be filed with each Co. "*Relevant date*", means the commencement of the Act as regards managing agents existing at the time, and if appointed subsequently, the date of such appointment. Penalty for default is a fine for partner in default (in case of firm), and the director or other officer in default (in case of body corporate).

Disclosure in Prospectus: Every prospectus and statement in lieu of prospectus must disclose names, addresses and description and occupation of managing agents, any provision in the articles or in any contract as to appointment of managing agent, the remuneration payable to him, and the compensation (if any) payable to him for loss of office, the dates of and parties to and general nature of every contract appointing or fixing remuneration of managing agent whenever entered into and full particulars of the nature and extent of the interest of managing agent in the promotion of or in the property proposed to be acquired by the Co.

Register of Managing Agent: Under s. 303, every Co. is bound to keep a register, *inter alia*, of managing agent, containing full particulars of his name, usual residential address, nationality, his business occupation, and any other offices held by him as director, managing director, managing agent, secretaries or treasurer or manager in other corporate bodies, and the date of his birth (the last is not necessary in case of non-

subsidiary private Co.). Similar particulars are to be entered if the managing agent is a body corporate or a firm, or a private Co. The Co. has also to send a return to the Registrar containing the above particulars within 28 days of the appointment of the first director. If a change occurs, the same should also be notified to the Registrar within 28 days of its happening. Penalty for default is fine for Co. and officer in default. Under s. 304, the register is to be kept open for inspection of members without charge and of non-members for a small fee. Every managing agent is, within 20 days of his appointment, bound to disclose to the Co. the particulars required to be mentioned by s. 303. Failure is punishable with fine (s. 305). The Registrar, under s. 306, is bound to keep a separate register, in which all the above particulars regarding the managing agent shall be entered.

Director's interest in appointment of managing agent: Where a Co. proposes to enter into any contract for the appointment of a managing agent in which a director is interested or concerned, or proposes to vary any such existing contract, the Co. shall send, along with an abstract of the terms or variation, a memo. clearly specifying the nature of the concern or interest of such director in the contract, to every member, in sufficient time before the general meeting at which the proposal is to be considered. If a director becomes interested or concerned after such contract is entered into, such abstract and memo. shall be sent to each member within 21 days of the date on which the director became concerned or interested. Penalty for default is fine for Co. and officer in default. Contract for the appointment of managing agent shall be kept at the registered office of the Co. and shall be open to inspection of members. Copies and extracts may also be taken therefrom, as in the case of register of members [s. 302(3) (4)].

Variation of managing agency agreement: A variation of terms of managing agency agreement must be sanctioned (i) by a resolution of the Co. in general meeting. (ii) It must also be sanctioned by the Central Government before such resolution is passed (s. 329). (iii) The term of office of all managing agents (if it does not expire earlier by reason of provisions of the previous Companies Act) shall expire on 15th August 1960 unless they are reappointed for a fresh term before that date as laid down by the Act. (iv) All provisions of the Act other than those relating to the term of office shall apply to managing agents existing at the commencement of the Act (s. 330). Notice that all the above provisions apply to public Co. and to private subsidiary thereof, and to non-subsidiary private Co.s also, unless these last are exempted by a Notification of the Central Government (s. 327).

Number of Managing Agencies: Under s. 332, after 15th August 1960, no person shall, at one time, hold more than 10 Managing Agencies. If a person fails to comply with the above requirement before the aforesaid date, the Central Government shall, after that date, determine which 10 managing agencies the person shall be permitted to keep. In calculating the number of 10, a private Co. (not being subsidiary or a holding Co. of a public Co.), an unlimited Co. and an association "not for profit" or prohibiting payment of dividend, shall be excluded. Persons holding office of managing agents, shall include, where they are a firm, every partner therein and where the managing agents are a Co., any director, secretaries and treasurers and manager thereof and any member thereof who is entitled to exercise not less than 1/20th of its total voting power. Contravention of the above, is punishable with a fine (upto Rs. 1,000 for every day for every Co. in excess of 10, for which such person acts a managing agent).

Managing Agents to have Charge on Assets: Where a managing agency agreement terminates under s. 324 or s. 332 (i.e. by abolition under Central Government Notification, or by reason of exceeding the maximum number of 10), the managing agent shall have a charge on the assets of the Co. for all moneys due to him from the Co. at the time or for which he may become liable thereafter in virtue of an obligation properly incurred by him on behalf of the Co. previously thereto, subject to all charges and incumbrances then existing thereon (s. 333).

Vacation of Office of Managing Agent

Under s. 334, a managing agent shall be deemed to have vacated his office, (i) if, being an individual, he is adjudicated insolvent, (ii) or if he applies to be adjudicated, (iii) if he is a firm, on the dissolution thereof, for any cause whatever, including insolvency

of a partner, (iv) if he is a body corporate, on the commencement of its own winding up, whether compulsory, voluntary or under supervision, and (v) in all cases, on the commencement of winding up of the Co., of which he is a managing agent, whether compulsory, voluntary or under supervision. (vi) A managing agent shall also be *deemed to have vacated office*, if he, his partner (if a firm), or a director or officer of a body corporate holding a general power of attorney on its behalf (if the managing agent is a body corporate), is convicted by an Indian Court after the commencement of the Act, and sentenced to imprisonment for not less than 6 months (s. 336). In case of a partner, director or officer falling under the above sec., if the managing agent dismisses or expels such person within 30 days of the sentence, the disqualification shall not apply (s. 341). In cases coming under cl. (i) of s. 334 and cases coming under s. 336 above, the disqualification shall not take effect for 30 days after the adjudication, appointment of receiver, sentence or finding; if an appeal is filed within the said period, until 7 days after the disposal of the appeal and in case of a further appeal within the aforesaid 7 days, until after the disposal thereof. The Board has further power to suspend the managing agent from office immediately on or after the adjudication, or appointment of receiver, or sentence or finding and until the disposal of the appeals and petitions referred to above or until the convicted partner, director or officer is expelled or dismissed under s. 341. (vii) Under s. 346, where a "change" as defined in the sec. takes place in the composition of the managing agency firm or body corporate and such managing agency firm or body corporate is managing agent of a public Co. or a private subsidiary thereof, the managing agent shall cease to act as such on expiry of 6 months of the date of "change" or such further time as may be allowed by the Central Government in that behalf, *unless*, before the expiry of the said period, approval of the Central Government has been obtained for the "change". Expulsion of a convicted partner under s. 341 will amount to such "change".

Suspension of Managing Agent: A managing agent shall be *deemed to be suspended from office*, if a receiver is appointed of his property (i) by a Court or (ii) by and on behalf of creditors of managing agent including holders of debentures issued by the managing agent in pursuance of an instrument executed by him. The Court which appointed the receiver, however, as also the Court which will have jurisdiction to wind up the Co., may, by its order, direct that the managing agent shall continue as such for such period and on such terms as the Court may specify. The Court may also cancel or vary such order (s. 335). The Board also has the power of suspending the managing agent from office immediately on or after adjudication, appointment of receiver, sentence or finding, referred to in cl. (1) (a) of that sec., and until the disposal of the appeals and petition referred to in cls. (b) and (c) of cl. (1) of the sec. or until the convicted partner, director or officer is expelled or dismissed under s. 341 [s. 340(2)].

Removal of Managing Agent: (1) A Co. in general meeting may, by *ordinary resolution*, remove a managing agent from office, (i) for fraud or breach of trust in connection with the affairs of the Co., or its subsidiary or holding Co., whether committed before or after the commencement of the Act, (ii) for fraud or breach of trust in relation to any other body corporate, whether committed before or after the commencement of the Act, if the same is established before a Court of Law, either within or outside India, and (iii) if any partner in his firm or if a body corporate, any director or officer holding general power of attorney on its behalf, is guilty of fraud or breach of trust referred to in (i) (s. 337). With regard to cases falling under (ii), the disqualification shall not take effect for 30 days after the sentence, and in case of an appeal within the said period until 7 days after the disposal of the appeal and in case of further appeal within such 7 days until the disposal thereof (s. 340). The Board has power to immediately suspend the managing agent also during the aforesaid period under the same sec. as stated before.

(2) A Co. in general meeting may by *special resolution*, remove a managing agent for gross negligence or gross misconduct in the affairs of the Co. or any subsidiary thereof (s. 338). For considering resolutions of the nature referred to in ss. 337 and 338 above, two directors are entitled to call a general meeting (s. 339). A copy of the resolution for removal of managing agent, on receipt thereof, shall be forthwith sent to the managing agent. In connection with such resolution, the managing agent shall have the same right as a director has under s. 284, with regard to a resolution for his

removal (*Ibid*), e.g. he can make representations in writing, may have them read out at the meeting and he may also be heard at the meeting.

Managing Agents are employees of the Co. and the Co. has therefore power to dismiss them from their office if they are guilty of misconduct (i). As the Privy Council pointed out in the above case, however, to justify the dismissal of a managing agent of a Co. on the ground of misconduct, the question to be considered is whether the misconduct proved or reasonably apprehended, has such a direct bearing on the employer's business or on the discharge by the employee of that part of the employer's business in which he is employed, as seriously to affect or threaten to affect the employer's business or the employees apparent discharge of his duty to his employer. The nature of the particular business and the nature of the duties of the employee require to be considered in each case in order to arrive at a just conclusion on the question. Where the misconduct proved consisted of quarrels between partners of the managing agent firm of such nature and duration as to seriously impair their capacity to discharge their duty to the Co. as managing agents and to prejudicially affect the interests of the Co., held, this was sufficient to justify the Co. to dismiss them from their position as managing agents (*Ibid*).

Resignation of Office By Managing Agent: A managing agent may resign office by notice to the Board from the date specified in the notice, unless the managing agency agreement otherwise provides. From the date specified in the notice or such other date as may be agreed upon, he shall cease to act as managing agent (s. 342). On notice of resignation being received, the Board shall prepare a statement of the affairs of the Co. as at the date specified in the notice of resignation, or such subsequent date as the directors think fit (not being later than the date fixed for the managing agent ceasing to act as such as aforesaid); together with a balance sheet duly made out to that date and profit and loss account of the Co., for a period subsequent to the date for which such profit and loss account was prepared and laid before the last general meeting and ending on that date, duly audited by auditors, and place the resignation, the balance sheet, profit and loss account and the auditor's report before the Co. in general meeting, which may thereupon accept such resignation or take such other action with reference thereto as thought proper. Only on such procedure being gone through, the resignation shall be effective. The auditor's report shall be read before the meeting and shall be open to inspection of member. The auditor shall be entitled to notice of such meeting and to be heard thereat on his report. Penalties prescribed by ss. 232 and 233 shall apply in all such cases.

Transfer and Succession to Managing Agency not permitted: A transfer of his office by a managing agent shall not take effect, unless approved both by the Co. in general meeting and by the Central Government (s. 343). Similarly, any agreement of managing agency entered into after the commencement of the Act, providing for succession to the office by inheritance or devise, shall be void. *This rule, however, does not apply to a private Co. (not being subsidiary of a public Co.) (s. 344).* As regards managing agency agreements, existing at the commencement of the Act providing for succession to office as above, they shall not be effective as regards such succession, unless the successor in question is approved by the Central Government, which shall not grant such approval, unless it is of opinion that he is a fit and proper person to hold such office. *This rule is also not applicable to a private Co. (not being subsidiary of a public Co.) (s. 345).*

Change in the Managing Agents' Constitution: Where, in case of a public Co. (or a private subsidiary thereof), a "change" occurs in the constitution of the managing agent's firm or in the body corporate constituting the managing agent, the managing agent shall cease to act as such on expiry of 6 months of the "change" (or such further term as the Central Government may allow), unless within such time, the approval of the Central Government is obtained to such "change". "Change" includes (i) conversion of a private into a public Co. and vice versa; (ii) any change in the directors or managers of the corporation, whether caused by death or retirement of director or manager or appointment of new director or manager or otherwise; (iii) any change

in ownership of shares in the body corporate or in the membership thereof (if it has no share capital). As regards a body corporate whose shares are dealt with or quoted on a recognised Stock Exchange, a "change" of ownership of its shares shall not be within the sec., unless the Central Government by notification, declares it so to be. The Central Government shall not issue such notification unless, in its opinion, the change of ownership which has taken place or is about to take place has affected or is likely to affect prejudicially the affairs of the managed Co. (s. 346).

Effect of Termination of Managing Agency: Where the office of managing agent ceases or is terminated, the managing agent and the Co. shall be entitled to enforce any claim or demand which each may have against the other, for acts and omissions committed before such termination. The rights and liabilities of the managing agent to the Co., in any other capacity, shall not be effected thereby. This sec. is new. It clarifies the position of the managing agent and the Co. *vis-à-vis* each other, on the termination of managing agency. It provides that mutual rights and liabilities between the two, shall remain unaffected by such termination (s. 367).

Contracts by Managing Agent: Where managing agent enters into any contract on behalf of the Co. in which the Co. is an undisclosed principal, he shall at the time of entering into the contract make a memo. in writing of its terms and of the person with whom the contract was entered into. The managing agent shall forthwith deliver the memo. to the Co. and send copies thereof to each director. The memo. shall be filed in the Co.'s office and shall be laid before the Board at its next meeting. If default is made in complying with the above requirements, the contract shall be voidable as against the Co. and the person entering into the contract and every officer in default will be punished by fine (s. 416).

Restrictions on Activities of Managing Agents

(1) Appointment as Selling Agent: No managing agent or his "associate" shall receive any commission or other remuneration for sale of goods produced by the managed Co. and sold, (i) at the premises at which the goods are produced, (ii) the head office of the managing agent, or (iii) from any place in India. As regards sales of such goods outside India (at places other than the above), a managing agent or his "associate" can be appointed selling agent of such goods provided (i) he maintains his own office at such place for his own business, unconnected with the business of the Co., (ii) the remuneration payable to him for such work is sanctioned by a *special resolution* of the Co. (which must set out the material terms of his appointment), and (iii) no other sums are payable by the Co. to him for such work, for expenses or otherwise. The appointment shall not be for more than 5 years at a time, but may be renewed during the last year of the term, for another similar period. Particulars of every such appointment must be entered in a register to be maintained by the Co. (s. 356). Where and in so far as the business of the Co. consists of supplying or rendering services to outsiders, the same rules as above shall apply as regards business procured for the Co. by the managing agent or his "associate" from places outside India (s. 357).

(2) Appointment as buying agent: No managing agent or his associate shall receive any payment whatever from the Co. for goods purchased on its behalf whether in India or outside (s. 358). Two exceptions to this rule are, however, recognised: (i) Under sub-sec. (i) of the sec., expenses sanctioned under s. 354 of the Act (see *ante*) can be paid by the Co. to him; (ii) under cl. (2) of the sec., as regards goods purchased by the managing agent or his associate outside India, if (a) the managing agent or his associate maintains an office at such place and (b) such office is maintained by him not only for the Co.'s business, but also for his own separate, distinct and independent business, then, he may at his option, receive (i) such part of the office expenses as may be reasonably attributed to the Co.'s business or (ii) remuneration by way of commission or otherwise for work done by him or his associate for such purchases. In case (i) above, the maximum amount payable shall be specified in a special resolution of the Co. In case (ii) above, the remuneration shall be payable in accordance with the terms of a special resolution passed in that behalf. The special resolution in each case must set out in detail the nature of the office maintained, the purposes for which it is maintained, the scale of its operations, expenses incurred in maintaining such

office and the proportion thereof which can be reasonably attributed to the work done on behalf of the Co. The special resolution shall remain in force for 3 years but may be renewed in the last year of its term for a further period of 3 years. Every resolution passed under the sec. shall be entered in a register to be maintained by the Co. for that purpose.

(3) **Commission to Managing Agent buying and selling for other concerns:** Under s. 359, a managing agent or his "associate" can retain commission or other remuneration earned or to be earned by him, as the managing agent, secretaries and treasurers, manager, secretary, agent or selling or buying agent, of another firm, corporation or concern, in respect of goods, power, freight, repairs or other services, for which contract has been or is to be entered into, by such bodies with the Co., provided: (i) such retainer is authorised by the managing agent's own Co. by resolution in general meeting and (ii) the rates charged by such bodies are not less favourable than the market rates or are otherwise reasonable. Every such contract, with all particulars thereof, shall be entered in a separate register to be maintained by the Co.

(4) **Contracts for sale, purchase, etc. between Managing Agent and Company:** Under s. 360, a Co. may, by *special resolution*, approve of any contract being entered into with its managing agent or his associate: (i) for the sale, purchase, or supply of movable or immovable property or for supplying or rendering any services (other than that of managing agent) or (ii) for underwriting shares or debentures to be issued or sold by the Co. The special resolution shall set out the material terms of the contract and further, shall specifically provide that for the property supplied or sold, or any services supplied or rendered by the Co., the managing agent or his "associate" shall make payment to the Co. within one month from the date of the supply or sale of the goods, or supply or rendering of the services, as the case may be. Every such contract, with full particulars thereof, shall be entered in a separate register to be maintained by the Co.

The provisions of the above sec. do not apply to contract or contracts for the sale, purchase, supply of any property or services, in which, either the Co. or the "associate" regularly trades or does business, provided the aggregate value thereof during the calendar year comprised in the contract, does not exceed Rs. 5,000 in all.

Existing contracts: All existing contracts at the commencement of the Act to which ss. 356-560 would apply, shall be deemed to be terminated on 1st March 1958, unless they terminate earlier (s. 361).

Registers: The registers referred to in ss. 356-560, shall be open to inspection, and extracts and copies can be taken therefrom, by any member in the same way and subject to the same conditions, as in case of register of members (s. 362).

All remuneration received in contravention of the above provisions by managing agent or his "associate", either directly or indirectly, by way of remuneration, rebate, commission, expenses or otherwise, shall be held in trust by him for the Co. and he shall be accountable to the Co. for the same as such (s. 363).

Assignment of or Charge on Managing Agent's Remuneration: Any assignment of or charge on the remuneration or a part thereof, effected by a managing agent shall be void as against the Co. The rights of managing agents *inter se*, and of persons other than the Co., are not affected (s. 364). Under the sec., what is prohibited is a voluntary charge or assignment of his remuneration by the managing agent. A compulsory sale, at the instance of a creditor, is a different thing altogether, and the sec. does not make such sale or attachment of remuneration by a creditor of the managing agent invalid. *Purshottamdas v. Baijnath*, A.I.R. 1941 Cal. 240.

Restrictions on Powers of Managing Agents

Managing Agents are generally appointed under an agreement with the Co. or by resolution of the Board of directors. The agreement or resolution specifies the powers which the Co. grants to the managing agent as regards management of the Co.'s affairs in consideration of his acting as managing agent of the Co. Under the Act, managing agency agreement or resolution appointing managing agent, must be registered with

the Registrar along with the Memo. and the articles. A copy thereof is also to be annexed to every copy of the articles under s. 192. If articles are not registered, a printed copy of every such agreement or resolution shall be forwarded to any member at his request on payment of Re. 1 (*ibid*).

(1) **Superintendence and Control of Directors:** S. 368 provides that after the commencement of the Act, the managing agent, whether appointed before or thereafter, shall exercise his powers: (i) subject to the superintendence, directions and control of the Board, (ii) subject to the provisions of the Memo. and the articles, and (iii) subject to the provisions of Schedule VII (see below).

(2) **Powers exercisable with approval of Board:** Under Schedule VII, the managing agent shall not exercise the following powers without obtaining the *previous approval of the Board*. These powers are: (a) power to appoint manager (but not to suspend or dismiss him), (b) power to appoint any officer or member of the staff of the Co., whose salary is payable out of the funds of the Co., on a remuneration exceeding the limit laid down by the Board in this behalf, (c) power to appoint as officer or member of the staff of the Co., whose salary is payable out of the funds of the Co., any *relative* of the managing agent or of his partner (if the managing agent is a firm) or of any director or member of the private Co. (if the managing agent is a private Co.), (d) power to purchase capital assets for the Co. except within the purchase price limit fixed by the Board, (e) power to sell capital assets of the Co. except within the sale price limits prescribed by the Board, (f) power to compound or give extension of time for satisfaction or payment of the Co.'s claim (including a debt due to it from or against the managing agent, or his "associate"), (g) power to compound, or give extension of time with regard to any claim of the managing agent or his "associate" against the Co., including a claim for debt claimed to be due from the Co.

Under the present Act, s. 292 prohibits directors from delegating their powers to issue debentures to any Committee of them, to the managing director, managing agent, secretaries and treasurers and manager. As regards investment of the Co.'s funds, such power can under s. 292(1) proviso, be delegated to, *inter alia*, the managing agent, subject to the terms mentioned, as may be fixed by a resolution of the Board at a Board meeting.

(3) **Loans to Managing Agents:** No public Co. (or a private subsidiary thereof), shall make any loan, give guarantee or provide security in connection with a loan, made by any other person to or to any other person by: (i) its managing agent or his "associate" or (ii) any body corporate (apart from above), as to which the Central Government declares its satisfaction that its Board, managing director, managing agent, secretaries and treasurers or manager, is or are, "accustomed to act according to the directions or instructions" of the managing agent or his "associate" (s. 369). Neither the above sec. nor s. 295, prejudices any credit given by the Co. to its managing agent for facilitating the Co.'s business, held by him in his own name, in any current account or accounts, subject to limits approved by the Board, but not exceeding Rs. 20,000 in the aggregate.

(4) **Loans to Companies under same management:** Under s. 370, no Co. (public or private), shall make any loan, give guarantee or provide security in connection with a loan made by any other person to or to any other person by any body corporate, which is "under the same management" as the lending Co., unless the same is authorised by a *special resolution of the lending Co.* This does not apply to loans made, guarantee given or security provided by a holding Co. to its subsidiary or by the managing agent or secretaries and treasurers to Co. under his or their management. Two corporate bodies shall be deemed to be "*under the same management*": (i) if the managing agent, secretaries and treasurers, managing director or manager of one body (and where the managing agent or secretaries and treasurers are a firm, any partner thereof, and where they are a private Co., any director thereof), is the managing agent, secretaries and treasurers, managing director or manager of the other body or a partner in the managing agent's or secretaries and treasurer's firm or a director thereof if they are a private Co., or (ii) if the majority of directors of one body constitute, or constituted at any time within the preceding 6 months, a majority of directors of the other body.

Penalty for contravention of the provisions of ss. 369 and 370, for every party involved, including the person to whom loan is made or in whose interest the guarantee or security is given, is a fine or simple imprisonment. No imprisonment is awardable, where the liability has been completely made good and it is to be proportionately awarded according as the same as partially made good. All the above persons, if knowingly parties, shall also be jointly and severally liable to make good the liability to the Co. to the extent it remains outstanding (s. 371).

(5) Purchase of "Group Companies" Shares, etc.: S. 372 explains the expression "*group companies*" as follows: "A body corporate shall be deemed to be in the same group as the investing Co. if: (i) the body corporate is the managing agent of the other or (ii) if the two bodies are "under the same management" as defined by s. 370. As regards such Co.s, the sec. provides that no Co. shall be entitled to subscribe for or purchase shares or debentures of any body corporate of the "same group", (i) for an amount exceeding 10 per cent of the subscribed capital of the latter body, and further, (ii) in no case shall such investment of the Co.'s funds in shares or debentures of the body corporate in the "same group", exceed in the aggregate, 20 per cent of the subscribed capital of the investing Co.; (iii) further, such investment must be sanctioned by a *unanimous resolution* of the directors present at a Board meeting, and being entitled to vote thereon. Notice of such resolution, to be moved at the meeting, must have been given to every director as laid down in s. 286. Investment exceeding the above limit, can only be made, after sanction of the investing Co. in general meeting and after the approval of the Central Government.

A register of all such inter-investments shall be maintained by the Co. at its registered office, showing with respect to each investment: (i) the name of the body corporate in which the investment is made, (ii) the date of the investment and (iii) the nature and extent thereof. These particulars must be entered in the register within 3 days of the making thereof. The register must be kept open for inspection of members and for taking extracts and copies therefrom, by them, in the same manner and subject to the same qualifications as register of members under s. 163. Every Co. shall, after the commencement of the Act, annex to each balance sheet, a list of bodies corporate which are in the "same group" as itself and in the shares or debentures whereof, it has invested the funds of the Co., together with particulars of the nature and extent of such investments, in case of each Co. within the group. Except the last provision, all the other provisions of the sec. shall apply to an investment Co. also, i.e. a Co. whose principal business is the acquisition of shares, stock, debentures or other securities.

The section however does not apply to: (i) banking Co., (ii) insurance Co., (iii) private Co. (unless subsidiary of a public Co.), (iv) to investments by a Holding Co. in its subsidiary, and (v) to investments by a managing agent or secretaries and treasurers in the Co. managed by him or them.

As regards investments made by Co.s after 1st April 1952, which would have required sanction of resolution of the investment Co. and approval of the Central Government, if the above sec. was then in force, such sanction and approval shall be acquired by the Co. with respect thereto, within 6 months of the commencement of the Act, and if such and in so far as such sanction and approval is not obtained, the Board of Directors of the Co. shall dispose them off, so far as they are in excess of the limits laid down in s. 372(2), within 2 years of the commencement of the Act (s. 373). Penalty for default as regards provisions of ss. 372 and 373 is a fine for every officer in default (s. 374).

(6) Managing Agent not to engage in Competing Business: Under s. 375, unless a Co. by *special resolution*, permits, a managing agent shall not "engage on his own account", in any business of the same nature and directly competing with the business of the Co. or its subsidiary. "Engage on his own account" includes carrying on business: (i) by a firm in which he is a partner, (ii) by a private Co. in which he, his partner, or if the managing agent is a private Co., any director and officer thereof (or any two or more of these together), are entitled to exercise or control at general meeting not less than 20 per cent of the total voting power thereof, or (iii) by a corporate body (other than a private Co.), at general meeting of which, not less than 70 per cent of the total voting power is exercised or controlled by the aforesaid persons or any two

or more of them. Profits and benefit of business carried on by managing agent in contravention of the above, shall be held by him in trust for the Co. or its subsidiary as the case may be, and where profits are received in trust for more than one Co., in trust for each, in such proportion as may be agreed upon or as may be decided by the Court.

(7) Restriction on Appointment of Directors by Managing Agent: Under s. 277, if authorised by articles, a managing agent shall have power to appoint not more than 2 directors, where the total number of directors exceeds 5, and 1 director, where it does not exceed 5. The managing agent shall have power, at any time, to remove such director and appoint another in his place or in place of such director resigning or vacating office otherwise. Provisions in any articles or agreement, authorising the managing agent to appoint more directors than as provided above, shall be void, after one month of the commencement of the Act. In such cases, the managing agent shall determine within the said month, which of such directors shall continue to hold office. If no such choice is made, all directors appointed by the managing agent shall be deemed to have vacated office after expiry of the said month. This sec. makes an important departure from the provisions of s. 87-I of the Act of 1913. Under the latter sec., managing agents were empowered to appoint 1/3rd of the total number of directors of public Co. as a maximum, whatever the total number may be. The present Act has substantially reduced the quota.

(8) Restriction against Amalgamation: Where, before or after the commencement of the Act, by the Memo., articles, resolution of the Board or of a Co. in general meeting or by any agreement, a reconstruction or amalgamation of the Co. is prohibited, except on condition that the managing director, managing agent, secretaries and treasurers or manager shall be appointed or reappointed as any such officers of the new Co., the said prohibition shall be void with effect from the commencement of the Act or shall be void when made (s. 376).

(9) Relief in case of Mismanagement by Managing Agent: Under ss. 397-407, apart from the right of a Co. to dismiss a managing agent for wrongful conduct, the Act now gives shareholders additional powers to apply to Court for relief against mismanagement by managing agent. The Central Government also can itself intervene to prevent such mismanagement under the conditions laid down by s. 408 of the Act (see *ante*). Similarly, the powers of investigation which are given by ss. 235-251 can also be invoked in a fit case against managing agent.

(10) Misfeasance: Misfeasance proceedings against managing agents can be taken in a fit case under s. 543 of the Act (see *seq.*).

SECRETARIES AND TREASURERS AND THEIR "ASSOCIATES"

Position of Secretaries and Treasurers: Ss. 378-383 of the present Act, give statutory recognition to a body of persons, who manage the affairs of a Co., in the same manner as Managing Agent does, but on a basis somewhat different from that of Managing Agent. While the Managing Agent usually undertakes the additional liability of financing or procuring finance for the Co. under his management, that responsibility is not ordinarily taken up, or intended to be taken up, by the Secretaries and Treasurers and who, therefore, do not claim and also, are not expected to claim, any share, large or small, in the fruits of their management beyond the maximum remuneration fixed by the Act for the purpose.

Appointment of Secretaries and Treasurers: S. 2(44) defines "Secretaries and Treasurers" as follows: "Secretaries and Treasurers means a firm or body corporate (not being the Managing Agent), which, subject to the superintendence, control and direction of the Board of directors, has the management of the whole or substantially the whole of the affairs of a Co. and includes any firm or body corporate, occupying the position of Secretaries and Treasurers, by whatever name called and whether under a contract of service or not."

As the sec. indicates, Secretaries and Treasurers are a firm or a body corporate. An individual, therefore, cannot occupy the position. They are not identical with but

are other than Managing Agents. In other words, they are to be a different body, from what managing agents are and have been. This fact is further emphasised by s. 378, which by its proviso adds that no Co. shall, at the same time, have both a managing agent and Secretaries and Treasurers. Thus Secretaries and Treasurers are an alternative body, which a Co. may appoint for the management of its affairs, in place of or in substitution of managing agents who have ceased to function or whom it does not choose to appoint for the purpose.

Secretaries and Treasurers may be appointed to act as such under a contract or otherwise. By what name they call themselves is not material. Provided they carry on the functions of Secretaries and Treasurers, they will be governed by the relevant provisions of the Act relating to such body. Their names, occupations and addresses must be disclosed in the prospectus and the statement in lieu of prospectus (s. 70 and s. 44).

Provisions in the articles or in any contract, irrespective of the time when it was entered into, as to their appointment and the remuneration payable to them, must also be disclosed in the said documents (see Schs. III and IV)

When a Director is interested or concerned in a contract entered into by the Co. for the appointment of Secretaries and Treasurers, the Co. under s. 302, is bound to send an abstract and memorandum to every member of the Co. clearly specifying the nature of such concern or interest of the director in question. It must be sent in sufficient time before the general meeting of the Co. at which the proposal is to be considered. The same rule applies when such a contract is varied.

All contracts entered into by the Co. for the appointment of Secretaries and Treasurers must be kept at the registered office of the Co. and shall be open to inspection of all members within reasonable limits (s. 302).

Full particulars of their names, nationality, occupation and addresses and also of any other office held by them in other Co.s as managing or other directors, managing agents, secretaries and treasurers, or managers, must also be entered in the register to be kept by the Co. under s. 303. The Co. must send a return to the Registrar in the prescribed form containing the above particulars and also notify any change among the secretaries and treasurers. All fresh appointments of secretaries and treasurers to managerial posts in other Co. must be notified to Co. by them within 20 days thereof under s. 305.

Powers and Functions: The Act has placed the same restrictions and limitations on the powers of Secretaries and Treasurers, as it has placed on those of managing agents, as it is obvious that they will normally perform the same functions which the managing agents performed in relation to the Co. This is made clear by s. 379, which provides that subject to certain exceptions mentioned therein, all the provisions of the Act, applicable to or in relation to Managing Agent which is a firm or body corporate, shall apply to Secretaries and Treasurers. The same is true with regard to provisions of the Act relating to "associates" of Managing Agents. Those provisions will, under the sec., equally apply to "associates" of Secretaries and Treasurers.

Exceptions: The provisions of the Act which do not apply to Secretaries and Treasurers under s. 379 are the following: (i) s. 324 which deals with abolition of Managing Agency by Central Government Notification under certain conditions, does not apply to Secretaries and Treasurers. (ii) Similarly, the provisions of s. 320, terminating all managing agencies by 15th August 1960, do not apply to Secretaries and Treasurers. (iii) The restriction that Managing Agents cannot act as such, for more than 10 Co.s at a time, also does not apply to them. The result is that Secretaries and Treasurers of a Co., if duly appointed, are entitled to hold office for the full term of their appointment, without fear of being expropriated before the expiry of their term, as is possible in case of Managing Agents. They can also act as such Secretaries and Treasurers for any number of Co.s they choose to select.

Power to appoint Directors: Secretaries and Treasurers have no power to appoint any ex-officio directors on the board of directors, as the Managing Agent has under s. 377 (s. 382). By parity of reasoning, the restrictions placed by s. 261, on appointment

to the Board of Directors, of persons, who are, or may be intimately connected with, the Managing Agents, do not apply in their case.

Selling and buying agents: S. 383 provides that unless and except to the extent to which they are authorised by the Board, Secretaries and Treasurers shall have no right to sell goods or articles produced by the Co. or to purchase machinery, stores, goods and materials for the Co. or to sell the same when no longer serviceable.

MANAGERIAL REMUNERATION

Under s. 198, save as otherwise provided by the Act, the total remuneration payable to directors, managing agents, secretaries and treasurers and manager (if any), of a public Co. (and of a private Co. which is subsidiary of a public Co.), shall not exceed 11 per cent of the net profits of the Co. as computed under ss. 349-351 of the Act, except that the remuneration payable to directors shall not be deducted from gross profits under the above secs. so far as total managerial remuneration is concerned. The percentage shall be exclusive of fees payable to directors for attending Board meetings. The above provision does not prevent the payment of monthly remuneration to directors and manager under ss. 309 and 387 respectively. They do not also affect the provisions of ss. 352-360. If in any financial year, the profits of a Co. are not enough to pay remuneration to the abovenamed persons on the aforesaid scale, the Co. may pay to any director or directors including managing or whole-time directors, if any, its managing agents or secretaries and treasurers, if any, or if there are two or more of them holding office in the Co., to all of them together, as minimum remuneration, a sum not exceeding Rs. 50,000 per annum as it considers reasonable.

The Central Government, however, is satisfied that for the efficient conduct of the Co.'s business, the minimum remuneration of Rs. 50,000 mentioned above is or will be insufficient in cases where a monthly payment is made or proposed to be made to a managing or whole-time director or directors and manager or to any one or more of them, the Central Government may, by order, sanction an increase of such minimum, to such sum, for such period and subject to such conditions (if any), as may be specified in the order.

The effect of the above provisions is to fix an annual overall ceiling for total managerial remuneration in respect of a Co. at 11 per cent of the net profits of the Co., with a fixed minimum in cases where the profits are inadequate and with power to the Central Government to increase the minimum, in cases where it is found that the same is not adequate, having regard to any managing or whole-time director or directors or manager employed by the Co. It is to be observed that it is the fixed minimum only, that the Central Government is empowered to increase. Further, it can so increase the fixed minimum only in cases where a salaried managing or whole-time director or directors or manager is employed by the Co. This provision is made, because a Co. which has been newly started, might require the services of a highly qualified Indian or foreign specialist or expert, to help it in its first operations, whose services, however, may not be available within the minimum limit fixed by the sec. It should be noted that the Central Government may increase the minimum in suitable cases, to any extent that may be necessary, e.g. even beyond the 11 per cent of the overall ceiling fixed by s. 198. Over and above the 11 per cent maximum, further payment of fees or monthly payment to directors for attending meetings of the Board is not prohibited (cl. 2).

Further, under cl. (3) of s. 309, additional remuneration can be paid to a director who is in the whole-time employment of the Co. or who is a managing director, in the shape of a specified percentage of the net profits of the Co. Under the sec., such percentage shall not exceed 5 per cent for any one such director and not exceed 10 per cent, where there are more than one such directors.

Further, under cl. (4) of s. 309, in case of any other director (i.e. director who is not in the whole-time employment of the Co. or who is not a managing director and who does not receive any monthly payment from the Co.), the Co. may authorise payment to him or if more than one, to all of them, together, of a commission not exceeding 1 per cent of the net profits, where they are managing or whole-time director or directors, managing agent, secretaries and treasurers or manager, and not exceeding 3 per cent

of the net profits, if there are none such, provided (i) the remuneration of such director does not include a monthly payment and (ii) a special resolution of the Co. is passed authorising such payment.

Cl. (6) of s. 309 further provides that no director of a Co. who receives commission from the Co. and who is either whole-time or managing director of the Co., shall receive any commission or other remuneration from its subsidiary. Apparently, a salaried whole-time or managing director of a Co. is not within the above prohibition.

Under cl. (8) of s. 309, the above provisions with regard to managerial remuneration, come into operation immediately on the commencement of the Act. Where the end of the financial year of a Co. does not coincide with such commencement, the provisions will be operative from the expiry of the financial year immediately succeeding such commencement. It is doubtful whether the last provision applies to the provisions laid down as to maximum total managerial remuneration fixed by s. 198 also, or whether the provisions of s. 198 are to be operative, immediately on the commencement of the Act, irrespective of the expiry date of the financial year of a Co.

Notice that none of the above provisions regarding managerial remuneration are applicable to non-subsidiary private Co. (cl. 9, s. 309).

In a recent Bombay case (*Ramabehn v. Messrs. Jyoti Ltd.*, 59 Bom. L.R. 67), a partner in the Managing Agent's firm, who was also a technical adviser of the Co. drawing a salary of Rs. 3,000 per month, was appointed a director of the Co. On a question having arisen as to whether (a) the salary payable to the newly appointed director, should be taken into account, in deciding whether the amount payable to him exceeded 5 per cent of the net profits referred to in s. 309(3), (b) whether the same should be taken into account in considering the 11 p.c. fixed by s. 198, and (c) whether the same should be considered for the purpose of limiting the managing agent's commission fixed at 10 p.c. under s. 348, *held*, that on a true construction of the respective secs., the salary payable did not come within the mischief of s. 309(3) or s. 198, but came within the mischief of sec. 348, and must therefore be taken into account in determining 10 p.c. payable to managing agents.

Method of Payment of Remuneration: As s. 198 provides, the remuneration payable to a director according to cl. (2) of s. 309 may be paid, either by way of monthly payment or by way of fee for each meeting of the Board or partly by one way and partly by the other. The remuneration payable shall be determined either by the articles or by a resolution or by a special resolution, if the articles so require (s. 309, cl. 1). Where a director's remuneration has been fixed by special resolution, the resolution shall remain in force for not more than five years, after which, however, it can be renewed for a further period, not exceeding five years. Such renewal can only be in the last year of its operation (s. 309, cl. 7).

Under s. 200, no Co. shall pay to any of its officer or employees, whether in their capacity as such or otherwise, remuneration free from any tax or otherwise calculated by reference to or varying with any tax payable by him or the rate or standard rate of any such tax or the amount thereof. "Tax" includes income-tax as well as super-tax. In case of existing officers or employees of the Co. who are entitled, under the terms of their appointment to a "tax-free" remuneration, cl. (2) of the sec. provides that the same shall be paid to them for the residue of their term, on the basis of a gross sum, which after deducting such tax (if taxable) would yield the net sum actually specified. The above restrictions do not however apply to remuneration which falls due before the commencement of the Act or which falls due thereafter, but in respect of a prior period.

Directors' Remuneration—How computed

Under cl. 1 of s. 198, the computation of "net profits" of the Co. for the purpose of fixing the directors' remuneration, where they are paid on a percentage basis, is to be made in the manner laid down by ss. 349-51 of the Act. As the cl. points out, however, so far as directors are concerned, the remuneration payable to a director shall not be deducted from the gross profits for arriving at the figure of "net profits" in accordance

with the above secs. In other cases, however, it has to be deducted. (For ss. 349-51 see seq.)

Under s. 310, in case of a public Co. (and a private subsidiary thereof), any amendment of the provision regarding remuneration of any director, including a whole-time or managing director, whether contained in the Memo., articles, agreement or resolution of the Co. or Board, which directly or indirectly increases the amount thereof, shall not be effective, unless approved by the Central Government and shall be void in so far as disapproved. Similarly, under s. 311, in case of a public Co. (and a private subsidiary thereof), if the terms of reappointment or appointment of a managing or whole-time director after the commencement of the Act increase, directly or indirectly, the remuneration payable to him beyond what he or his predecessor was receiving before such reappointment or appointment, the appointment or reappointment shall be of no effect unless approved by the Central Government and shall be void so far as disapproved.

Compensation to Director for Loss of Office: Ss. 318-321 lay down elaborate provisions for regularising payment of compensation to directors for loss of office. Under s. 318, such compensation can be paid *only* to a managing director, director holding the office of manager and to a whole-time employee director and to no others. The compensation payable shall be on the basis of average remuneration actually earned by such persons for 3 years (or such shorter period as may be the case), immediately preceding the ceasing of holding of such office, and shall be for the unexpired portion of his term or for 3 years (whichever is shorter). No such payment, however, can be made at all, if winding up of the Co. has commenced before or commences within 12 months after he ceased to hold office, if the assets on winding up (after deducting expenses of winding up), are not sufficient to repay the shareholders the capital contributed by them (inclusive of premium, if any).

No payment of such compensation can also be made in the following cases: (i) where the director resigns office due to reconstruction or amalgamation of the Co. with another body or bodies corporate and such director is appointed managing director, managing agent, secretaries and treasurers, manager or other officer in the resulting new body; (ii) where the director resigns otherwise than as above; (iii) where the director vacates office under s. 203 (acting fraudulently as director or manager), s. 280 (superannuation), or s. 283(1), cls. (a)-(k) (vacation of office by director); (iv) where winding up (compulsory, voluntary or under supervision) has been due to the negligence or default of the director in question; (v) where the director has been guilty of any fraud, breach of trust in relation to or gross negligence or gross mismanagement of the affairs of the Co. or any subsidiary or holding Co. thereof; (vi) where the director has instigated or taken part directly or indirectly in bringing about the termination of his office. Payment of remuneration to a managing director or director manager for service rendered by him in other capacities is not prohibited.

S. 319 further provides that no director of a Co. shall, in connection with the transfer of the whole or any part of the undertaking or property of the Co., receive any payment as compensation for loss of office or as consideration for retirement from office or in connection with such loss or retirement either from the Co. or from the transferee, or from any other person, *unless* particulars with regard to such payment, together with the amount thereof have been disclosed to the Co. and the proposal has been approved by the Co. in general meeting. Payment received by a director in contravention of the above shall be held by the director as trustee for the Co.

Compensation to Director for loss of office owing to transfer of shares: A director might be offered compensation for loss of office by interested parties when a large stock of the Co.'s share capital is sought to be acquired by such parties for their own private purposes. Receipt of such compensation by any director on such transfer of shares is prohibited by s. 320, except under stringent conditions. The sec. provides that, when a transfer of any or all shares of the Co. is made to any person, as a result of: (i) an offer to the general body of shareholders or (ii) an offer made by another corporate body, in order that the Co. may become subsidiary of that other body or of the latter's holding Co., (iii) an offer made by an individual with a view to obtain control of not less than 1/3rd of the total voting power at the general meeting of the Co., or (iv) any other offer which is conditional to a given extent on acceptance, no director shall accept

compensation for or in connection with loss of office or for or in connection with retirement from office from (i) the Co. or (ii) except as provided hereafter, from the transferee or (iii) any other person. In the last two cases, the director can do so only after taking all reasonable steps to secure that full particulars of the proposed payment (including the amount) are included in or sent with the notice to the shareholders with regard to the offer in question. If the director in question fails to take such steps or if the person properly required by him to give such notice fails to do so, both of them are punishable with fine (upto Rs. 250).

If the steps regarding notifying the members of the Co. as mentioned before are not taken by the directors or if the proposed payment to the director is not, before the transfer of the said shares, approved by a meeting, specially called for that purpose of the same class of shareholders (being other than holders of shares held by the offeror or his nominee or if the offeror is a Co., by the Co., its nominee or subsidiary), the director shall hold the amount so paid to him in pursuance of the offer, as trustee for the holders of shares which have been sold, and he shall not be able to retain thereout the expenses of distributing the same to the persons concerned. If a meeting called for the purpose of such approval, is adjourned for want of quorum and at the adjourned date also, the quorum is not present, the payment shall be deemed to have been approved.

Under s. 321, where in proceedings started for recovering payments held by a director as trustee under s. 319 or s. 320, it is shown that (i) the payment was in pursuance of an arrangement for the transfer in question or was made within 1 year before or 2 years after the agreement or offer and (ii) that the Co. or the transferee was privy thereto, the payment shall be presumed to be covered by the said secs., unless the contrary is shown. Similarly, if the price paid to a director whose office is abolished or who is to retire from office, for shares held by him, in connection with a transfer to which s. 319 or s. 320 applies, appears to be more than the market price of similar shares or if any valuable consideration is given to such director, the excess or consideration shall be deemed to be "compensation for loss of office or retirement from office or in connection thereof", for the purpose of the above secs. The abovenamed payments do not include *bona fide* payment of damages for breach of contract or for pension for past services (including superannuation allowance or superannuation gratuity or like payments). Other rules of law, requiring disclosure as regards such or similar payments made or to be made to a director, are not affected by the above rules.

Remuneration of Managing Agent

Ss. 348-355 of the Act lay down provisions for regulating the remuneration payable to Managing Agents. None of the provision applies, however, to non-subsidiary private Co. (s. 355). The above provisions of the Act lay down an almost complete and comprehensive code for calculating the amount of remuneration payable to Managing Agents as such in any given case. With an overall ceiling of 10 per cent and with a composite set of rules, both of a positive as well as negative nature, no difficulty should now arise on the question of the quantum of managing agents' remuneration.

S. 348 provides that save as otherwise provided by the Act, no Co. shall pay to its managing agent for any financial year beginning at or after the commencement of the Act as remuneration, for acting as such or in any other capacity, *more than 10 per cent of the "net profits"* of that financial year.

"Net profits", how computed: Credits allowed and disallowed: S. 349 lays down how such "net profits" shall be computed. It provides as follows: *Credit shall be given for:* (i) bounties and (ii) subsidies received from Government or any constituted public authority authorised by any Government (unless the Central Government otherwise directs), *but credit shall not be given for:* (i) premiums received on shares or debentures issued or sold by the Co., (ii) profits on sales of forfeited shares, (iii) profits from sale of any undertaking or undertakings of the Co. or part thereof, and lastly, (iv) profits from sale of any immovable property or fixed assets of a capital nature comprised in any undertaking or undertakings of the Co. (unless buying and selling such property or assets is wholly or partly the business of the Co.).

Debits allowed and disallowed: The following items *shall also be deducted*: (i) usual working charges, (ii) director's remuneration, (iii) bonus payable or paid to member of the Co.'s staff, engineer, technician or person employed by the Co. on whole or part-time basis, (iv) any tax notified by the Central Government as being in the nature of a tax on excess or abnormal profits, (v) any tax on business profits imposed by Central Government for special reasons or in special circumstances and notified in this behalf by the same, (vi) interest on debentures, (vii) interest on mortgages executed by the Co. and on loans and advances secured by a charge on its fixed or floating assets, (viii) interest on unsecured loans and advances, (ix) repairs to movable or immovable property, if not of a capital nature, (x) outgoing, (xi) depreciation as laid down by s. 350, (xii) loss (not being of a capital nature), incurred in any year which begins at or after the commencement of the Act, which has not been taken into account in computing net profits in that year or any subsequent year preceding the year in question, (xiii) compensation or damages payable under any legal liability, including breach of contract, (xiv) charges for insurance against the risk of liability under (xiii) above. The following items, however, *shall not be deducted*: (i) remuneration payable to managing agent, (ii) income-tax and super-tax payable by the Co. under the Indian Income-tax Act of 1922 or any other tax, other than excess or abnormal profit tax, and special business profits tax mentioned in cls. (iv) and (v) above and (iii) compensation or damages paid voluntarily, i.e. otherwise than in virtue of a legal liability.

In cases of Profit-sharing: S. 351 further provides that where there is a profit-sharing arrangement between two or more Co.s, and not less than two of such Co.s have the same managing agent, profits paid by any of the Co.s having that managing agent to any other or others of them, under such arrangement, shall not be included in computing the "net profits" of paying Co. but shall be included in the "net profits" of the receiving Co. or each of the receiving Co.s to the extent of the payment received by it.

Additional Remuneration when payable: Additional remuneration beyond what is provided by s. 198 and s. 348 shall be paid to managing agent if and only if: (i) the same is sanctioned by the Co. by a *special resolution* and (ii) is approved by the Central Government as being in public interest (s. 352). Remuneration to managing agent for any financial year or part thereof shall not be paid until the accounts of the Co. for the financial year in question have been audited and laid before the Co. in general meeting. The minimum fixed under s. 198, however, can be paid in such instalments as may be provided for by the articles or resolution at annual general meeting or in the managing agency agreement (s. 353).

No office allowance: No office allowance shall be paid to managing agent but he shall be entitled to be reimbursed of all expenses incurred by him on behalf of the Co., and sanctioned by the Board or by the Co. in general meeting (s. 354).

Depreciation: Under s. 350, "depreciation" for the above purpose shall mean the normal depreciation allowed for this item under the Income-tax Act for the particular financial year, but *shall not include*: (i) special, initial, or other depreciation, or any development rebate (allowed under the Income-tax Act or otherwise), (ii) arrears of depreciation may be taken into account in the first financial year under s. 348, if not already taken into account for computing net profits in preceding financial years.

Compensation to Managing Agent for Loss of Office: S. 363 provides that no Co. shall pay or be liable to pay compensation to a managing agent for loss of office in the following cases: (i) where managing agent resigns office on reconstruction or amalgamation and is appointed managing agent, secretaries and treasurers, manager or other officer in the new corporate body, (ii) where he resigns office otherwise, (iii) where he vacates office under ss. 324, 330 or 332, (iv) when he is deemed to vacate office under s. 334 (cls. a, b, c and d), and under s. 336; (v) where he is deemed to vacate office under s. 334(e), provided the winding up has been caused by his negligence or default, (vi) where he is suspended or deemed to be suspended from office under s. 340(2), (vii) where he is removed from office under s. 337 or 338 and (viii) where he has instigated or taken part in the termination of his office.

Barring the above cases, compensation for loss of office may be paid by a Co. to its managing agent, but under s. 368, such compensation shall not exceed the remunera-

tion he would have earned if his term had continued for the residue of his term or for 3 years (whichever is less). The amount is to be calculated on the average remuneration actually earned by him in the preceding 3 years or lesser period, during which he held office. If the winding up of the Co. has begun before his office is terminated as above, or if it begins within 12 months thereof, no compensation shall be payable to him unless the share capital contributed by members (including premium), as well as the winding up expenses have been repaid to them in full, in winding up.

Notwithstanding termination of office, the mutual claims and demands of the Co. and the managing agent between themselves for anything done or not done, shall remain unaffected. Similarly, the rights and liabilities of the managing agent to the Co. in any other capacity shall also remain unaffected (s. 367).

Remuneration for Secretaries and Treasurers: This is fixed by s. 381 at $7\frac{1}{2}$ per cent maximum, of the "net profits" of a particular year. Other provisions relating to managing agents as regards remuneration are also applicable to them, under s. 379. All the provisions, however, are subject to s. 198 fixing the overall managerial remuneration at 11 per cent.

Managing Agent and Manager distinguished: A manager can only be an individual, a managing agent can be a Co., a firm or an individual. The manager is administratively under the control and supervision of the directors. The control over managing agent would be exercised by the directors only in terms of the agreement appointing him (j). The Managing Director derives from an agreement with the Co. the powers of management which need not necessarily extend to the whole or even substantially the whole of the Co.'s affairs. They may in fact be limited to a particular aspect of its affairs. A manager is merely an executive, acting under the direct day-to-day orders and directions of the directors. Differing provisions are also laid down by the new Act defining their respective rights, obligations and responsibilities.

Manager

Definition: Manager has been defined by s. 2(24), as "an individual (not being the Managing Agent) who, subject to the superintendence, control and direction of the Board of Directors, has the management of the whole or substantially the whole of the affairs of a Co. and includes a director or any other person occupying the position of Manager, by whatever name called, and whether under a contract of service or not". A Manager in order to be manager, must have the management of the whole or substantially the whole of the affairs of the Co. Thus the manager of a branch office will not be within the definition. The name under which a manager works or by which a manager is called makes no difference. A director acting as "manager" will be liable for all the liabilities of a manager under the Act.

Appointment of Manager: Under s. 384, no firm or body corporate or association can be appointed manager of a public Co. or a private subsidiary thereof, after the commencement of the Act. As regards such firms or bodies corporate or associations, as are working as manager at the commencement of the Act, they shall cease to function as such, 6 months after such commencement. Under s. 388 (which applies s. 317 to a manager), a public Co. and a private subsidiary thereof, cannot appoint a manager for more than 5 years at a time. He may be appointed for a further term of 5 years but such reappointment must be made not earlier than two years before the same is to come into force.

Under s. 385, the following persons, after the commencement of the Act, shall not be appointed or continue to be employed as managers of Co.s: (i) an undischarged insolvent or person adjudged insolvent within 5 preceding years, (ii) a person who suspends or has suspended payment to creditors within preceding 5 years or who compounds or has compounded with his creditors within a similar period, (iii) a person who is or has been within preceding 5 years convicted by an Indian Court of an offence involving moral turpitude. The Central Government may by notification remove the above disqualification generally or with regard to particular specified Co.s.

Number of Managements: S. 386 provides that after the commencement of the Act, no Co. shall employ or continue to employ as its manager, a person who is a manager or Managing Director of more than one other Co. With regard to such last employment also, it must be sanctioned by a unanimous resolution, at a Board meeting, of all directors present thereat, notice of the meeting and of the resolution to be passed thereat having been specifically given to all directors then in India. When at the commencement of the Act, a person is holding office of either manager or managing director in more than 2 Co.s, he shall within 1 year thereof, choose any two Co.s from them in which he wishes to hold office of manager or managing director and the provisions of s. 276, with regard to directors shall, with necessary modifications, apply to such case also. The Central Government may permit, by order, any person to be appointed manager of three or more Co.s, if satisfied that for their proper working, they should function as a single unit with a common manager. The above provisions do not apply to private Co. (unless subsidiary of a public Co.).

Remuneration: Under s. 387, the remuneration payable to a manager shall, subject to s. 198, be by monthly payment or by specified percentage, *not exceeding 5 per cent* of "net profits", calculated as laid down in ss. 349-351 or partly by one and partly the other way. Under s. 388 (which applies ss. 310 and 311 to manager also), any amendment of a provision relating to remuneration payable to a manager which directly or indirectly has the effect of increasing the amount thereof, whether contained in the Memo., articles, an agreement, or resolution, shall be void, if not approved by the Central Government. Similarly, if the appointment or reappointment of a manager involves increase of remuneration payable to him, such appointment or reappointment shall have no effect, unless approved by the Central Government. Both the above provisions do not apply to private non-subsidiary. No assignment of office can be made by a manager after the commencement of the Act.

Secretary

Definition: A "secretary" is defined by s. 2, cl. (45), as meaning "the person, if any, who is appointed to perform the duties which may be performed by a secretary under this Act".

Appointment: The Act does not make the appointment of a secretary to the Co. obligatory. Where a Co. wants to appoint a secretary, it is generally done by a resolution of the directors. If there are special terms of appointment a written agreement is entered into. Specific performance of a contract of personal service cannot be enforced [s. 21(b), Specific Relief Act] (k). If there is a clear negative covenant, however, it will be enforced by injunction (l).

Position of Secretary: A secretary is a servant of the Co. and as such servant is bound to carry out the duties assigned to him by the Co. Being a mere servant, he has no authority to represent anything at all. An agreement between him and the Co., does not prevent the Co. from appointing a general manager (m).

Officer, who is: Important provisions are, for the first time, introduced by the present Act regarding the appointment, powers and liabilities of various "officers" of a Co. An "officer" under the Act has wide connotation. As s. 2(30) lays down, "officer" "includes any director, managing agent, secretaries and treasurers, manager or secretary" of the Co. and "where the managing agent or secretaries and treasurers are a firm also includes any partner in the firm and where the managing agent or secretaries and treasurers are a body corporate, also includes any director, managing agent, secretaries and treasurers or manager of the body corporate". As regards an *auditor*, however, the cl. provides that *except* for ss. 477-478 (power to summon persons suspected of having Co.'s property and power to order public examination), s. 539 (penalty for falsification of books), s. 543 (power of Court to assess damages against delinquent directors), s. 545 (prosecution of delinquent officer), s. 621 (cognisability of offence under the Act),

(k) *Stocker v. Brocklebank* (1851) M. & G.

250. (l) *Lumley v. Wagner* (1852) 1 De.G.M.

& G. 604.

(m) *Krishna v. Indo. Union Ass.* (1944) Com. Ca. 10.

s. 625 (compensation to officers in case of frivolous complaint), and s. 633 (power of Court to grant relief to officers and others), an *auditor is not to be regarded as an officer of the Co.*

Rules as to appointment of officers: Under ss. 368, 379, read with Sch. VII, neither the managing agent nor the secretaries and treasurers of a Co., can appoint a manager without the previous sanction of the Board, though they can suspend him or even dismiss him from service. They cannot also appoint, without the previous sanction of the Board, any officer on a scale of remuneration beyond the maximum laid down by the Board, in cases in which such remuneration is payable out of the funds of the Co. They cannot also appoint, without the previous sanction of the Board, any "relative" of the managing agent or secretaries and treasurers (as the case may be). Where the managing agent or secretaries and treasurers are a firm, no partner of such firm, and if they are a private Co., no director or member thereof, can be similarly appointed, without prior sanction of the Board. What is to happen where managing agent or secretaries and treasurers are a public Co. is not mentioned. The result of the above provisions is that, except in the cases mentioned above (and subject to other provisions of the Act), the managing agent or secretaries and treasurers have full power to appoint officers of the Co. and to suspend and dismiss them, provided their agreement with the Co. does not place any limit on such power. Under s. 204, after the commencement of the Act, no firm or body corporate shall be appointed or employed to or in an office or place of profit (as defined by s. 314), under the Co. (excepting the office of managing agent or secretary and treasurer) for a term of over five years at a time. This restriction however does not apply to the appointment or employment of such bodies as technicians or consultants; but will apply, if such body employed as aforesaid, is already the managing agent or secretaries and treasurers of the Co. or a partner of these persons (being a firm) or a director or member of a private Co. (composed of the aforesaid persons) or a director of any other Co. (composed of the said persons).

Any firm or corporate body holding an office of profit in a Co. as aforesaid at the commencement of the Act shall vacate the same after 5 years of such commencement, unless their time expires earlier. The sec. does not prohibit the re-appointment, re-employment or extension of the term of office of such bodies for a further period, not exceeding 5 years each time, such extension and re-appointment however must be sanctioned within the last two years of the term. *The section does not apply to a private Co., unless subsidiary of a public Co.*

Under s. 294, the directors of a Co. (public as well as private), cannot appoint anyone as sole selling agent of the Co., for any area, except on condition that such appointment shall be invalid if not approved by the Co. in general meeting within 6 months of such appointment. As regards existing sole selling agencies, the sec. provides that, where the period extends to 5 years or more, the appointment shall be placed for confirmation before a general meeting of the Co. within 6 months of the commencement of the Act. The Co. in general meeting may either (i) ratify the appointment or (ii) terminate the same as follows: if the appointment is made on or after 15th February 1955, terminate it forthwith or from a date specified in the resolution and if made before that date, terminate the same, with effect from not less than 5 years of the date of appointment or less than 1 year of the commencement of the Act (whichever is later) as may be specified in the resolution. Notice that existing appointments of sole selling agents, where such appointments have been made for less than 5 years, are left untouched by the above provisions. Presumably, they are to be allowed to run their contractual period without confirmation by the Co. in general meeting being necessary. No limits are apparently placed on the remuneration payable to such sole selling agents or on any other term of their appointment.

Under s. 314, certain persons cannot hold office or place of profit under the Co., unless their appointment is sanctioned by a special resolution of the Co. They are (i) a director, (ii) a partner or "relative" of a director, (iii) any firm in which such director or "relative" is a partner, (iv) any private Co. in which such director is member or director, and (v) the managing agent, secretaries and treasurers, and manager of such private Co. as is mentioned in (iv) above. The above prohibition operates in cases of subsidiaries of the Co. also, unless remuneration payable to such person by

the subsidiary is paid over by him to the holding Co. Holding the following offices, however, does not require prior sanction of a special resolution of the Co.: that of managing director, managing agent, secretaries and treasurers, manager, legal adviser, technical adviser, banker or trustee for debenture-holders. "Holding office or place of profit" is also defined (see *ante*).

Under s. 200, no payment of remuneration to an officer or employee as such or otherwise shall be free of "tax" or be calculated by reference to or varying with any tax or rate of tax or amount thereof. "Tax" includes income-tax and super-tax.

As regards remuneration payable to officers and employees at the commencement of the Act under any contract or resolution of the Co. or Board, on tax-free basis, the same shall be payable to them for the residue of their term except that payment to them shall be on the basis of a gross sum which subject to the "tax" would yield the net sum payable to them before. The last provision will not apply to commission which fell due before the commencement of the Act or which is for a period before such commencement, but falls due thereafter.

Security Deposits, Provident Fund, Salaries and Wages

Under s. 417, all security deposits made by employees of a Co. under the terms of their contracts must be kept or deposited by the Co. in a special account to be opened in a Scheduled Bank. The Co. cannot use such securities or moneys for purposes other than those agreed to under the relevant contracts. A receipt for moneys deposited as above shall not be regarded as a security itself.

As regards provident funds, s. 418 provides that where a Co. has constituted a provident fund, for its employees or any class of them, all moneys contributed to such fund (by the employee or the employer), or accruing by way of interest or otherwise to such fund, shall be deposited by the Co. in a Post Office Savings Bank Account or invested in trust securities. Where 1/10th of the whole amount of the fund exceeds the maximum which can be deposited in Post Office Savings Bank Account under its rules, the excess may be kept or deposited in a special account in a Scheduled Bank.

No employee shall in respect of the amount to his credit in such fund shall receive interest at a rate exceeding the rate of interest yielded on such investment. The employee shall be entitled to obtain advances from or withdraw money standing to his credit in the fund where such fund is a recognised provident fund under s. 58A of the Income-tax Act or where the rules of the fund contain rules similar to rules 4-9 of the Income-tax (Provident Fund Relief) Rules. Where a Co. creates a separate trust with regard to any provident fund, the Co. shall be bound to collect contributions of the employees concerned and pay such contributions as well as its own contributions, if any, to the trustees. Other obligations with regard to such trust shall devolve on the trustees.

Under s. 419, every employee shall, on request, be entitled to see the Bank's receipt for any money or security deposited in a Scheduled Bank as aforesaid. Penalty for default in complying with the provisions of ss. 417-419 is fine (upto Rs. 500) for officer of Co. or trustee knowingly guilty of the same (s. 420).

A Full Bench of the Allahabad High Court has laid down the following test for determining whether a "deposit" of money with a Co. by way of "security deposit" constitutes a "trust" or not. "A fair test of whether a sum of money of this kind is to be held as a trust fund or not is to ask whether in the circumstances, it was intended that it should remain a segregated fund or whether it should, on payment, be the property of the Co. and be compensated for by the Co.'s express or implied covenant to repay it in exactly the same way as the customer's deposit in a bank creates the relationship of debtor and creditor (*n*).

Preferential Payment of Salaries and Wages: Where a Co. is wound up, (i) all wages and salaries of employees (including wages for time or piece-work and salaries

earned wholly or in part by way of commission), for period not exceeding 4 months within twelve months of the commencement of winding up, not exceeding Rs. 1,000, (ii) all holiday remuneration becoming payable to an employee or in case of his death, to another person in his right, on the termination of his appointment owing to winding up, (iii) all amounts payable by the Co. as employer under the Employees' State Insurance Act, 1948, or any other law in force during 12 months next before winding up (except in case of voluntary winding up for amalgamation or reconstruction), (iv) amounts payable to workman in respect of compensation under the Workmen's Compensation Act for death or disablement, unless the Co. is being voluntarily wound up for amalgamation or reconstruction or unless the Co. is under such a contract with any Insurance Co. as would transfer all such rights to the workman in question under s. 14 of the above Act, and (v) all sums due to employee from provident fund, pension fund, gratuity fund or other fund for the welfare of the employees maintained by the Co., must be paid in priority to all other debts of the Co. (s. 530).

ARBITRATION, COMPROMISE AND ARRANGEMENT WITH MEMBERS AND CREDITORS

References to Arbitration: A Co. may, by written agreement, refer any present or future dispute between itself and another Co. or person, to arbitration in accordance with the Arbitration Act of 1940. A Co., when party to arbitration, may delegate to the arbitrator, power to settle any terms or determine any matter which can be lawfully settled or determined by the Co., the Board, managing director, director, managing agent, secretaries and treasurers or manager. The provisions of the Arbitration Act shall apply to all such arbitrations (s. 389).

Schemes of Arrangement and Compromise with Creditors and Members: S. 391, cl. (1), provides that where a "compromise" or "arrangement" is proposed: (a) between a Co. and its creditors or any class of them or (b) between a Co. and its members or any class of them, the Court, on the application of the Co., creditor, member or liquidator (if the Co. is being wound up), order a meeting of the creditors or class of creditors, members or class of members (as the case may be), to be called and conducted in such manner as the Court directs.

Under cl. (2), if at such meeting (i) a majority in number (ii) representing $\frac{3}{4}$ ths in value of the creditors or class of creditors, members or class of members (as the case may be), (iii) present and (iv) voting in person or by proxy (where proxies are allowed), (v) agree to the compromise or arrangement, the same shall, (vi) if sanctioned by the Court, be binding on all creditors or class of them, members or class of them (as the case may be), and also on the Co. and on the liquidator and contributories (if the Co. is being wound up): Under cl. (3), a certified copy of the Court's order shall be filed with the Registrar and the scheme shall have no effect till then. A copy of the order shall be annexed to every copy of the Memo. issued after the filing of the order (if the Co. has no Memo., to every copy of its constitution issued thereafter) (cl. 4). On failure to do so, the Co. and every officer in default is punishable with fine (upto Rs. 10) for each defaulting copy (cl. 5). When application has been made under the sec., the Court has power to stay the commencement or continuation of any suit or proceedings against the Co., on terms (cl. 6).

An appeal lies against order made under the sec. by a Court of original jurisdiction, to the Court hearing appeals therefrom. The same rules as regards filing and annexing copies shall apply to such appellate orders (cl. 7).

Under s. 390, cl. (a), "company" in the above sec. and s. 393 means "any company liable to be wound up under the Act; similarly under cl. (b) of the same, "arrangement" includes reorganisation of the share capital of a Co. by consolidation of shares of different classes or by division of shares into shares of different classes or by both the methods. Further, under cl. (c), for the purposes of the above secs., "unsecured creditors" who have obtained decrees, shall be deemed to be of the same class as unsecured creditors who have not obtained such decrees.

Powers of Court when sanctioning Schemes of Arrangement and Compromise: S. 392 gives power to the Court sanctioning a compromise or arrangement (i) to supervise

the carrying out thereof, and (ii) at the time of sanctioning or thereafter, to give necessary directions with regard to any connected matter and (iii) to make such modification in the compromise or arrangement as may be necessary for the proper working thereof. If the sanctioning Court is satisfied that the compromise or arrangement with or without modification cannot be worked satisfactorily, the Court, on its own motion or on application of any person interested in the affairs of the Co., may make a winding up order which shall be deemed to be an order under s. 433. The sec. applies to all orders made under s. 153 of the Companies Act of 1913.

Procedure at meeting under s. 391: Under s. 393, notice of every meeting called under s. 391 which is sent to a creditor or member shall also contain a statement of the terms of the arrangement or compromise and in particular, any material interest therein of the directors, managing director, managing agent, secretaries and treasurers or manager (whether as members, creditors or otherwise) and the special effect (if any) of such interest on the compromise or arrangement in question. If notice is given by advertisement, the notice must include the aforesaid particulars or specify the place and manner where creditors or members concerned may obtain copies thereof. Where the compromise or arrangement affects the rights of debenture-holders, similar information and explanation shall be given with regard to the scheme to the trustees of such debenture-holders. Where copies of the statement are declared to be available, every creditor or member concerned shall, on application, be entitled to a copy thereof, free of charge. In case of default under the sec., the Co. and every officer in default, and the liquidator and trustee for debenture-holder in default, shall be punishable with fine unless the person in question shows that default was due to a refusal of the relevant person to supply necessary particulars of his material interest. The above-mentioned persons are bound to give notice of their material interests for the above purpose. Penalty for failure is a fine.

Principles for granting Sanction: The principles which should guide the Court in granting sanction to a scheme brought before it were laid down by Lindley J. in *Re Alabama New Orleans, etc. Rly. Co.* (o) as follows: "What the Court has to do is to see, first of all, that the provisions of the statute have been complied with, and secondly, that the majority has been acting *bona fide*. The Court has also to see that the minority is not being overridden by a majority, having interests of its own clashing with those of the minority whom they seek to coerce. Further than that the Court has to look at the scheme and see whether it is one as to which persons acting honestly take a view which can be reasonably taken by businessmen". As to whether a scheme is of the above type or not, it has been held that it is a question of which shareholders acting honestly are better judges as to what is to their commercial advantage than the Court can be (p). A scheme which involves reduction of capital must be carried out according to the statutory provisions relating to reduction (q). Cl. (2) allows the decision of the majority to bind the minority and therefore it is incumbent on the Court to see that their decision does not act oppressively on the minority. In *Pramila Devi v. Peoples Bank of N. India* (r), the Privy Council held that a scheme sanctioned by the Court under the sec. has the force of a judicial pronouncement and becomes binding upon the shareholders and creditors alike of the Co. Its terms can thereafter be varied by the Court only after the variation has been approved by the necessary meetings of shareholders and creditors. No variation or departure from the scheme therefore can be validated by mere acquiescence of shareholders and creditors.

Appeal: An order sanctioning a scheme is appealable (s). A person, however, who may become a prospective beneficiary under a scheme if sanctioned but who is neither a creditor nor a shareholder of the Co., has no right of appeal against an order of the Court rejecting the scheme (t).

Composition in case of Banking Companies: Under s. 45 of the Banking Companies Act (10 of 1949), a compromise or arrangement between a Banking Company and its

(o) (1891) 2 Ch. 213.

(p) *Re English, Scottish & Australian Chartered Bank* (1893) 3 Ch. 385.

(q) *Re Cooper* (1902) W.N. 199.

(r) A.I.R. (1938) P.C. 284.

(s) *Re Mymansingh Loan Office Ltd.*, 41 C.W.N. 599.

(t) *Motilal v. Natvarlal*, A.I.R. (1932) Bom. 78.

creditors or members or any class thereof, shall not be sanctioned by any Court unless the same has been certified by the Reserve Bank "as not being detrimental to the interest of the depositors" of the Co. This is an additional requirement to be fulfilled before an arrangement or compromise relating to a Banking Co. can be sanctioned by the Court. In absence of such a certificate, therefore, such a scheme cannot be sanctioned by the Court. The powers of the Reserve Bank under s. 45, however, as regards granting of the certificate are limited. It has no power under the sec. to make substantial alterations in the scheme which is approved by the necessary majorities under the Companies Act. It was so held by the Calcutta High Court in *Bengal Bank v. Suresh Chakravarti (u)*. The Court pointed out that sec. 45 of the Banking Companies Act does not empower the Reserve Bank to modify a scheme in material particulars. Its power to grant a certificate is limited only to certifying that the scheme is not detrimental to the interests of the depositors of the Co. If the Reserve Bank in granting the certificate goes beyond its powers and modifies the scheme generally in material particulars it would amount to a refusal to grant a certificate. The Court also will have no jurisdiction to sanction a scheme so modified.

RECONSTRUCTION AND AMALGAMATION

Amalgamation—What is: The word "amalgamation" has no definite legal meaning. As Buckley says (Companies Act, 11th Ed., p. 487): "it contemplates a state of things under which two Cos. are so joined together as to form a third entity or one Co. is absorbed into and blended with another Co." As Romer, L.J. pointed out in *In re Walker's Settlement (v)*, "two Cos. can amalgamate in either of two ways. Co. A can sell its business and undertaking to Co. B in consideration of shares in Co. B. Co. A then goes into liquidation and distributes the shares in Co. B amongst its shareholders, and the result of it all is that whereas there were previously two corporations A and B, corporation A has now merged in corporation B. There is only one corporation carrying on one undertaking, with one set of shareholders. Another way in which it is frequently done is that a third Co., a new Co. C is formed and both the Cos. A and B sell their undertakings to Co. C in consideration of shares in undertaking C. The shares in A and B are then distributed amongst the shareholders by means of liquidation and the Cos. A and B cease to exist. As a result of the transaction there is now a new corporation C in place of the former corporations A and B. There is one set of shareholders instead of two sets of shareholders, one undertaking instead of two undertakings."

S. 394, cl. (1), provides that where an application is made to the Court under s. 391 for sanctioning a compromise or arrangement as therein mentioned, and it is further shown (a) that the same is for the purpose of or in connection with a scheme for reconstruction of any Co. or Cos., or (b) the amalgamation of two or more Cos., and that under such scheme, the whole or part of the undertaking, properties or liability of any Co. concerned in the scheme is to be transferred to another Co., the Court may, at the time of sanctioning the compromise or arrangement or by a subsequent order, provide for the following: (i) the transfer by the transferor Co. to the transferee Co. of the whole or part of the undertaking, property or liabilities of the former Co.; (ii) the allotment or appropriation by the transferee Co. of shares, debentures, policies or other like interests, in such Co. to or for any person as provided under the terms of the compromise or arrangement; (iii) the continuation by or against the transferee Co. of legal proceedings pending by or against the transferor Co.; (iv) the dissolution of the transferor Co. without winding up; (v) provision for members who, within the time and in the manner specified by the Court, dissent from the compromise or arrangement; and (vi) all incidental, consequential and supplementary matters, necessary for effectively carrying out the compromise or arrangement.

Under cl. (2), the Court's order directing transfer will automatically vest the transferred properties, etc. in the transferee Co. The Court may also direct such transfer to be free from any charge, if the compromise or arrangement provides for the same. Under cl. (3), a certified copy of the Court's order shall, within 14 days thereof, be filed with the Registrar by every Co. in relation to which the order is made. Penalty for default is a fine for Co. and officer in default. Cl. (4) further provides that "pro-

(u) A.I.R. (1948) Cal. 242.

(v) (1935) 1 Ch. 567, 583

perty" under the sec. includes property, rights and powers of all descriptions. "Liabilities" include duties of every description. "Transferor company" includes any body corporate, whether a "company" within the Act or not, but "transferee company" does not include any Co. other than a Co. under the Act.

Acquiring Shares of dissentient Members: Where a scheme involves a transfer of shares of one Co. to another as part thereof, it is possible that there may be members of the transferor Co. who either do not agree to the transfer or the terms thereof. Such members have to be provided for. S. 395 lays down the provisions relating to such a contingency. In short the sec. provides for compulsory acquisition of such members' interest by the transferee Co. on terms which are fair and equitable, "*Dissenting shareholder*" according to cl. 5(a) of the sec. includes (i) one who has not assented to the scheme or contract for transfer and (ii) any shareholder who has failed or refused to transfer his share to the transferee Co. in terms of the compromise or arrangement. Cl. (1) of the sec. provides (i) that where a scheme or contract involves a transfer of shares (or any class of shares) of a Co. to another Co., and the said scheme or offer has, within 4 months of the making thereof by the transferee Co., been approved by holders of not less than 9/10ths in value of the shares (or class of shares) of the transferor Co., the transferee Co. may, within 2 months of the expiry of the said period of 4 months, give notice to any dissenting shareholder of the transferor Co., that it desires to acquire his shares. If such notice is given, the transferee Co. shall be entitled and bound to acquire those shares on the same terms on which the shares of the approving shareholders are to be transferred under the scheme or contract, unless, within one month of the notice, the dissenting shareholder applies to the Court, and the Court otherwise directs. In calculating the ratio of 9/10ths, shares of the transferor Co. which are held, at the date of the offer, by the transferee Co., its nominee or subsidiary are to be excluded. The *proviso* to cl. (1) lays down that where such holding of the shares of the same class of the transferor Co. by the transferee Co. exceeds 1/10th of the aggregate value of all shares of that class in the transferor Co., the above provisions will apply, only if (a) the transferee Co. offers the same terms to all the members of the same class (excepting those held by itself) and further (b) if the scheme or contract is approved, not only by 9/10ths of the value of shares of the transferor Co. of the same class (exclusive of shares held by the transferee Co. as aforesaid), but also, by not less than 3/4ths in number of such holders of that class. This provision is introduced in order to correct the effects of undue weightage of the transferee Co.'s holding of the transferor Co.'s shares, where it exceeds 1/10th of the total value of those shares.

Cl. (2) provides that where in pursuance of such a scheme or contract as above, shares or shares of any class, are transferred to another Co. or its nominee and those shares together with other shares or other shares of the same class already held by the transferee Co. or its nominee or subsidiary, exceed 9/10ths in value of the shares or shares of the class transferred, the transferee Co., within one month of the date of the transfer, shall give notice of the fact in the prescribed manner, to the holders of the remainder of those shares of the transferor Co. who have not assented to the scheme or contract and thereupon the holders of such shares may, within 3 months of the notice, require the transferee Co. to acquire the shares in question. Where such notice has been given by the shareholders, the transferee Co. shall be entitled and bound to acquire the shares on the terms on which the shares of the approving shareholders were transferred or on agreed terms, or on such other terms as the Court orders, on an application in that behalf being made by the transferee Co. or the shareholders.

Cl. (3) provides that where the transferee Co. has given the above notice and the Court has made no order to the contrary, on the application of the dissenting shareholder, the transferee Co., on expiry of one month from the notice (and if application has been made to the Court, on expiry of one month from disposal thereof), transmit to the transferor Co., a copy of the notice, together with a transfer executed on behalf of the shareholder by an appointee of the transferee Co., and by the transferee Co. itself, in respect of the shares to be acquired and pay the price thereof to the transferor Co. The latter thereupon shall register the transferee Co. as the holder of these shares. No transfer shall be required in case of shares for which share warrant is outstanding.

Under cl. (4), all sums received by the transferor Co. under the sec. shall be paid into a separate Bank account and shall be held by the Co. on trust for the several shareholders entitled to the same. Under Cl. (5) (b), "transferor Company" in the sec. includes any body corporate, whether a Co. under the Act or not. "Transferee Company" includes only a Co. under the Act. Cl. (6) provides that where an offer has been made before the commencement of the Act, the above provisions shall apply with the following modifications: The ratio of 9/10ths and 1/10th in cl. (1) shall be inclusive of the transferee Co.'s holding of shares of transferor Co. cl. (2) shall not apply. Provisions for execution of transfer by the transferee Co.'s appointee, etc. shall be omitted. "Transferor" and "transferee" Co. shall include any body corporate, whether a "Company" under the Act or not

Nature of Jurisdiction: The function of the Court under the English corresponding sec. was described by Eve J. in *Re Castner-Kallner Alkali Co. (w)*, as follows: "The function of the Court is to determine on what terms the dissentients are to be dispossessed of their investment. There is nothing in the section to control the nature of the offer that the applicants may put forward, it is for the Court to consider and decide whether it is an adequate and satisfactory one and if not, to substitute such other terms of purchase as in its discretion are fair and just. The would-be purchasers do not lose their statutory rights by making an inadequate or otherwise unacceptable offer. The fact that the petitioners are offering to the dissentient's shares wholly different from those which were offered to the assenting majority does not deprive them of the opportunity to purchase the dissentient's shares. The language of the section expressly contemplates a difference between the terms fixed by the Court for the dissentients and those provided by the scheme"

Amalgamation at the instance of the Central Government: S. 396 provides that where in the national interest, it appears to the Central Government that it is essential that two or more Co.s should amalgamate, the Central Government may, by order, notified in the Official Gazette, provide for the amalgamation of the said Co.s into a single Co., with such constitution, property, powers, rights, interests, authorities and privileges and with such liabilities, duties and obligations as may be specified in the order. Incidental, consequential and supplemental provisions necessary to give effect to the amalgamation may also be included in the order. Every member and creditor of the amalgamated Co.s (including debenture-holders thereof), shall have the same interests in and rights against the amalgamated Co. as they had against the original Co.s. To the extent that their interest in or right against the amalgamated Co. is less than their original interest in or right against the original Co., they shall be entitled to compensation from the amalgamated Co. to be assessed by the prescribed authority.

No order can be made under the sec. unless, (i) draft copy of the proposed order is sent to each of the Co.s concerned and (ii) the Central Government has considered any suggestions, objections or modifications to the same to be made by the said Co.s and class of shareholders thereof and creditors thereof, within a period to be prescribed (not being less than 2 months from receipt of the draft order). Copies of orders passed under the sec. shall, as soon as may be thereafter, be placed before both Houses of Parliament. This sec. is entirely new.

ADVISORY COMMISSION

For enabling the Central Government to discharge efficiently the multitudinous duties which the Central Government has taken upon itself under the Act, ss. 410-415 provide for the constitution and functioning of an Advisory Commission, which will advise the Central Government as regards various matters referred to in the secs.

Duties of Commission: S. 410 provides for the appointment of such Advisory Commission by the Central Government. It is to consist of not more than 5 persons having suitable qualifications, one of whom will be appointed Chairman. The duties of this Commission, under s. 411, will be to advise the Central Government: (i) before a notification is issued under s. 324 (prohibiting appointment of managing agents for certain industries or businesses) as to the necessity and advisability thereof, (ii) on applica-

tions made to the Central Government under s. 259 (increase in number of directors), s. 268 (modification of provisions relating to managing, whole-time and non-rotational directors), s. 269 (appointment of managing or whole-time director), s. 310 and s. 311 (increase in remuneration of managing and other directors), s. 326 and s. 328 (appointment of managing agent), s. 329 (varying the terms of managing agency agreement), s. 332 (appointment of managing agent beyond 15th August 1960), s. 343 and s. 345 (transfer of and succession to managing agent), s. 352 (additional remuneration for managing agent), s. 408 (preventing oppression of members), s. 409 (preventing change in the Board) and (iii) on all other matters referred to it by the Central Government.

Applications under cl. 2, s. 411 above, shall be in prescribed form. Before making any such application to the Central Government, a general notice shall be issued by the Co. to the members indicating the nature of the application. Copies of such notice shall be published once in local newspaper in the language of the district in which the Co.'s registered office is situated and once in any English newspaper circulating therein. Copies of such notices with certificate of the Co. as to due publication thereof shall be attached to the application. Rules as regards notice to members and publication thereof do not apply to private Co. which is not the managing agent of a public Co. (s. 412).

Powers of Advisory Commission: Under s. 413, the Commission for purposes of inquiry may (i) require books and documents relating to matters under inquiry in the possession of the Co. to be produced, (ii) call for further information or explanation in order to get necessary particulars from the said books and documents, (iii) with the help of assistants, inspect and take copies of and extracts from the same, and (iv) require any managing or other director, managing agents, secretaries and treasurers, manager, shareholder or any other person likely to furnish information relating to matter under inquiry, to appear before it and examine him on oath for purposes of such information. Penalty for disobeying any requisition of the Commission as regards the above matters is punishable with imprisonment (upto 2 years) and fine (s. 414). Immunity from liability is granted to the Commission and the Central Government for all acts done in good faith in pursuance of the above by s. 415.

WINDING UP

Winding up generally: An incorporated Co. duly registered under the Act, can reach a termination of its existence in either of two ways: either by being wound up in the manner laid down by the Act or by its name being removed from the Register as a defunct Co. A Co. may go into liquidation for a variety of reasons. It may not be able to meet its obligations, it may desire a reconstruction of its framework or it may want to close down and divide the assets amongst the members. Liquidation or "winding up" as it is called, can be had in three ways: as provided by s. 425 (i) by the Court (ss. 433-483) or (ii) voluntarily (ss. 484-521) or (iii) under the supervision of the Court (ss. 522-527). Each of these three forms of winding up are different and involve different kinds of procedure (see below). The provisions of the Act relating to winding up, unless the contrary appears, apply to all the three modes of winding up. The following Co.s can be wound up under the Act: (i) Co.s formed and registered under the Act, (ii) Co.s registered but not formed under the Companies Acts of 1857, 1860 and 1882, and (iii) unregistered Co.s.

Winding up and Bankruptcy: It should be observed that winding up of a Co. is not the same thing as the bankruptcy of a Co.: (i) a winding up order can be made, even when the Co. is solvent, e.g. for purposes of reconstruction; (ii) on winding up, the Co., as such, does not cease to exist, only its administration is carried on through the medium of a liquidator (x). The property of the Co. still belongs to the Co., which can carry on business (for a limited purpose) and file suits in its own name. It is otherwise, in case of insolvency. (iii) Even where a Co. is ordered to be wound up because it is in insolvent circumstances, all the provisions of Insolvency Law do not apply to the case, but some only (see ss. 469, 574, 529, 531 and 533). Note that the rule as to "reputed ownership" in insolvency does not apply to Co.s in winding up (y).

(x) *Dawson's Bank v. Nippon Mankwa Kaisha*, 37 Bom. L.R. 544.

(y) *Gorring's v. Irovillox Works* (1884) 34 Ch.D. 129.

New Liability on Winding up: In the event of the Co. being wound up, the liability of those who were its members at the time of winding up, undergoes a legal change, and a new liability comes into existence. Before the winding up, they were liable only as "members" or "shareholders"; after the winding up, they become "contributories", with a liability to contribute to the assets of the Co., to an amount sufficient to pay the debts and liabilities of the Co., and costs, charges and expenses of winding up and of adjusting their rights amongst themselves, but in no case exceeding the amount remaining unpaid on the shares held by them or their guarantee, as the case may be. The new liability that arises in a winding up is not confined to those who were members at the time of winding up, but extends to those who were members of the Co. in the past, i.e. within 1 year of the winding up. All the persons who thus, on a winding up, become liable to "contribute" as stated above, to the assets of the Co., are called "contributories". The fact that this liability of contributories is a new liability was pointed out by the Privy Council in *Hansraj Gupta v. Asthana* (2). The liability arises "ex legis" and not "ex contractu". It is a statutory liability arising after winding up has started (*Ibid*). It has been held, therefore, that it is no answer to a liquidator's claim against any person whose name appears on the register as member, that there was an agreement with the directors to exclude this statutory liability (a).

Contributories

According to sec. 428, the term "contributory" means "every person liable to contribute to the assets of a Co. in the event of its being wound up, including the holder of a fully paid-up share (new) and in all proceedings for determining and in all proceedings prior to the final determination of the persons who are to be deemed contributories, includes any person alleged to be a contributory". The newly added words now make it quite clear that a fully paid-up shareholder is also to be regarded as a "contributory" and therefore entitled to exercise all the rights of a contributory, including the right to file a winding up petition (b).

Nature of the Liability of Contributory: Under s. 429, the liability of a contributory shall create a debt accruing due from him at the time when his liability commenced but payable at the time specified in the calls made on him for enforcing the liability. The sec. further provides that no claim founded on the liability of a contributory shall be cognizable by any Court of Small Causes sitting outside the Presidency Towns. The liability of a "contributory" creates a "debt", the "debt" accruing from the time the liability arose, i.e. on the commencement of liability but it is not "payable" at once, it is "payable" at the time specified in the calls made on him for enforcing the liability. The above rule has this important result that no limitation runs against a "contributory" till a liquidator is appointed and calls are made by him (c).

Limitation for Calls in Winding up: As pointed out by Chagla C.J. in *Mahomed Akbar v. Associated Banking Corporation of India* (d), a distinction has to be made between a call made before liquidation and enforcement of such pre-liquidation liability for the same against a member by the liquidator, and a call made by a liquidator in respect of the new liability of the member as contributory, which arises for the first time on liquidation by operation of the rule of law mentioned above. If the liquidator is seeking to enforce a pre-liquidation liability on the part of a shareholder for unpaid calls made before liquidation, the period of limitation for enforcing the same by suit is 3 years under Art. 112 of the Limitation Act.

If, on the other hand, the liquidator is seeking to enforce the new "ex leges" liability on the part of a member which arises on liquidation, by making of a call, in respect of the amount remaining unpaid on his shares, the period of limitation for enforcing such liability is 6 years under Art. 120 of the Limitation Act (e).

Extent of Liability of Contributory: S. 426 provides that in the event of a Co. being wound up, every "present" and "past" member, shall be liable to contribute to the

(2) 60 I.A. 13.

(d) *Geoffray Cornewallis v. Sikdar Iron Works Ltd.*, 59 Cal. 1099.

(b) *Re Aidall Ltd.* (1933) Ch. 323.

(c) *Re Union Bank of Allahabad*, 47 All. 669.

(d) 52 Bom. L.R. 599.

(e) (*Ibid*).

assets of the Co. to an amount sufficient to pay the debts and liabilities and the costs, charges and expenses of winding up and for the adjustment of the rights of contributories among themselves, *subject to the provisions of s. 427 (unlimited liability of directors and others)* and subject to the following conditions: (i) A "past" member shall not be liable to contribute, if he has ceased to be a member for one year or upwards before the commencement of the winding up. (ii) A "past" member shall not be liable to contribute in respect of any debt and liability of the Co. incurred after he ceased to be a member. (iii) A "past" member shall not be liable to contribute, unless it appears to the Court that the present members are unable to satisfy the contributions required to be made by them in pursuance of the Act. (iv) In the case of a Co. limited by shares, no contribution shall be required from any member exceeding the amount (if any) unpaid on shares in respect to which he is liable as a "present" or "past" member. (v) In the case of a Co. limited by guarantee, no contribution shall be required from any past or present member, exceeding the amount undertaken to be contributed by him to the assets of the Co. in the event of its being wound up. (vi) Nothing in the Act shall invalidate any provision contained in a policy of insurance or other contract, whereby the liability of the individual members on the policy or contract is restricted or whereby the funds of the Co. are alone made liable in respect of the policy or contract. (vii) Any sum due to any past or present member of a Co. in his character of a member, by way of dividends, profits or otherwise, shall not be deemed to be a debt of the Co. payable to that member, in a case of competition between himself and any other creditor who is not a past or present member of the Co., but any such sum may be taken into account for the purpose of final adjustment of the rights of the contributories among themselves. (viii) In the winding up of a Co. limited by guarantee, which has a share capital, every member of the Co. shall be liable, in addition to the amount undertaken to be contributed by him to the assets of the Co. in the event of its being wound up, to contribute to the extent of any sums unpaid on any shares held by him. Notice that under s. 45 a member is liable for all the debts of the Co., if he was aware that the number was reduced below 7 in case of a public, and below 2, in case of a private Co.

The above sec. defines the extent of the liability of contributories. After making a winding up order the Court generally settles a list of contributories (s. 467). This list consists of (i) present and (ii) past members of the Co. It is generally in two parts, the "A List" of contributories, comprising the present and existing members of the Co. and the "B List" consisting of "past members" of the Co., who are liable only in certain events. As regards *present members*, i.e. those whose names appear as members on the register of members at the date of the winding up, they are, as a matter of course, liable for the debts and liabilities of the Co., but there is this further rule that no contribution can be demanded from them exceeding the amount, if any, unpaid on their shares in the case of a Co. limited by shares and in case of a guarantee Co., in excess of the amount of their guarantee. As regards "*past members*", the term does not include all persons who have been members of a Co. in the past but as s. 426 above indicates, only those who have been members of the Co., within a year of the winding up order (though no longer members then). The liability of a "past member" or "B list contributory", therefore, is limited by the following conditions: (i) he is not liable to contribute if he has ceased to be a member for one year or upwards before the winding up commences; (ii) he is not liable to contribute for any debt or liability of the Co. incurred after he ceased to be a member; (iii) he is not liable to contribute unless it appears to the Court that the present members are unable to satisfy the contributions required to be made by them; (iv) in no case he is liable to contribute more than the amount (if any) unpaid on his shares or the amount of his guarantee. It is in this sense that it is said that the liability of the "B list" contributory is "secondary" while that of the "A list" contributory is "primary".

Extent of Liability of Directors, etc. whose Liability is Unlimited: On the winding up of a limited Co., the liability of any director, *managing agent, secretaries and treasurers or manager* (new) (whether past or present), whose liability is, in pursuance of the Act, unlimited, shall in addition to his liability (if any), to contribute as an ordinary member, extend to making a further contribution as if he were, at the commencement of the winding up, a member of an unlimited Co., subject, however, to the

the Court in that: (i) A past director, *managing agent, secretaries and treasurers* will not order (new) shall not be liable to make such further contribution if he has the Cl., provd office for a year or upwards before the commencement of the winding under this past director, *managing agent, secretaries and treasurers or manager* (new) on business liable to make such further contribution in respect of any debt or liability to remove. contracted after he ceased to hold such office. (iii) Subject to the articles, a *past, managing agent, secretaries and treasurers or manager* (new) shall not be liable to make such contribution unless the Court deems it necessary to require that contribution in order to satisfy the debts and liabilities of the Co. and the costs, charges and expenses of the winding up (s. 427).

Death of Contributory: If a contributory dies either before or after he is placed on the list of contributories, his legal representatives and his heirs shall be liable in due course of administration to contribute to the assets of the Co. in discharge of his liability and shall be contributories accordingly. If the legal representatives or heirs make default in paying any money ordered to be paid by them, proceedings may be taken for administering the property of the deceased contributory, whether movable or immovable or both, and of compelling payment thereof of the money due. For the purposes of the sec., the surviving coparceners of a contributory who is a member of a Joint Hindu family governed by the Mitakshara, shall be deemed to be his legal representatives and heirs. Mitakshara School includes all schools and sub-schools of Hindu Law except the Dayabhaga School (s. 430) (f). The liability is not personal, but extends only to the assets of the deceased shareholder which have come to their hands. The liquidator is not required to take out letters of Administration of the estate of a deceased contributory before he can make his estate liable for the contribution. The legal representatives of a legal representative of a deceased contributory are also held to be "contributories" under the sec. (g).

Insolvency of Contributory: Where a contributory is adjudicated insolvent, either before or after he is placed on the list of contributories, s. 436 provides that his assignees shall represent him for all purposes of winding up and shall be contributories accordingly and may be called on to admit to proof against the estate of the Insolvent or otherwise to allow to be paid out of his assets, in due course of law, any money due from the Insolvent in respect of his liability to contribute to the assets of the Co. and there may be proved against the assets of the Insolvent, the estimated value of his liability to future calls as well as calls already made. If a shareholder has been adjudicated insolvent his name cannot be placed on the list of contributories. The name of the Official Assignee of his estate also cannot be placed on the list, if he has disclaimed (h).

Contributories where a Member who is a body corporate is wound up: Under s. 432, where a body corporate is a member and that is wound up, whether before or after it is placed on the list of contributories, the liquidator of the body corporate shall represent that body for all purposes of winding up. He may be called upon to admit to proof against its assets or otherwise called upon to pay thereout according to Law all sums due by such body to the Co. in respect of its liability as such contributory. Estimated value of future calls may also be proved against the assets of such body in liquidation.

Consequences of Winding up

Important consequences result from a Co. being wound up. They may be summed up as follows: (a) As regards the Co. itself, winding up does not mean that the Co. has ceased to exist. The Co. exists as a corporate entity with all the rights of such entity, only its management and administration shall thenceforth be carried on through liquidators (see *ante*). (b) As regards the shareholders: (i) a new statutory liability as "contributories" comes into existence (see *ante*). They will be classified into "A" and "B" lists, with respective liability. (ii) Every transfer of shares or alteration in the status of a shareholder after the winding up has commenced shall be void, unless with the sanction of the Court or Liquidator (s. 536) (see *seq.*) (c) As regards the

(f) Jagmohan Das v. Off. Liq., A.I.R. (1956) All. 1045.

(g) Re Krishnaswami (1949) 2 Mad. L.J.

180.

(h) Re West of England Bank, 12 Ch.D.

288.

creditors, (i) they cannot file or continue suits against the Co. except v and the costs, the Court (s. 466). (ii) They cannot proceed with execution if they^{ts} of contri-decrees already (s. 537). (iii) They must lodge their claim and prove their liability of the Liquidator (as regards proof and payment of debts, see seq.). (d) " member servants of the Co., a winding up order by the Court operates as notice of tr or up- of their employment (s. 445). They can, of course, prove for any claim for all not for wrongful termination of employment which they have. A voluntary windur he does not necessarily operate as a notice of discharge (i). (e) As regards the director., managing agents, secretaries and treasurers and manager, their powers come to an end, except as far as allowed by the Court or the Committee of Inspection (s. 505). The same is true of other officers of the Co. also. (f) As regards disposition of Co.'s property, all such dispositions are void unless with leave of the Court or the Liquidator (s. 536). (g) Certain special rights of avoidance, investigation and punishment arise, once a Co. has gone into liquidation (see s. 531, and ss. 533-537 see seq.).

WINDING UP BY COURT

When Company may be wound up by Court: Ss. 433-434 of the Act deal with the subject of winding up by the Court or as it is sometimes called "compulsory winding up". S. 433 provides that a Co. may be wound up by the Court (a) if the Co. has by special resolution resolved that the Co. be wound up by the Court; (b) if default is made in delivering Statutory report to the Registrar or in holding the Statutory meeting; (c) if the Co. does not commence its business within a year from its incorporation or suspends its business for a whole year; (d) if the number of members is reduced, in case of a private Co. below two and in the case of any other Co., below seven; (e) if the Co. is "unable to pay its debts"; (f) if the Court is of opinion that it is just and equitable that the Co. should be wound up.

Under s. 434, a Co. shall be deemed to be "unable to pay its debts", (a) if a creditor, by assignment or otherwise, to whom the Co. is indebted in a sum exceeding five hundred rupees then due, has served on the Co. (by causing it to be delivered) at the registered office or by registered post or otherwise, a demand "under his hand", requiring the Co. to pay the sum so due and the Co. has for three weeks thereafter, neglected to pay the sum or to secure or compound for it, to the reasonable satisfaction of the creditor. The demand referred to above shall be deemed to have been duly "given under the hand of the creditor", if it is signed by an agent or legal adviser, duly authorised on his behalf or in the case of a firm, if it is signed by such agent or legal adviser or any member of the firm on behalf of the firm; or (b) if execution or other process issued on a decree or order of any Court in favour of a creditor of the Co. is returned unsatisfied in whole or in part, or (c) if it is proved to the satisfaction of the Court that Co. is "unable to pay its debts" and in determining whether a Co. is "unable to pay its debts", the Court shall take into account the contingent and prospective liabilities of the Co. The powers of the Court to compulsorily wind up a Co. are governed by ss. 433-434 of the Act. The Court can order the winding up of a limited Co. only in the cases mentioned in s. 433. It can do so on a petition either of a creditor or a contributory of the Co. (see below).

Failure to hold Statutory Meeting: As regards cl. (b), the Court has power under s. 543 to order the filing of the Statutory Report and of holding of the Statutory Meeting, instead of ordering a compulsory winding up. A creditor who is bound by a scheme sanctioned by the Court, has been held competent to petition for winding up on the ground that no Statutory meeting has been held and that no Statutory report has been filed (j).

Failure to carry on Business: As regards cl. (c), the power of the Court to order a compulsory winding up of a Co. which has not carried on business for a year is discretionary. It will not be exercised if there are indications that the Co. honestly wants to carry on business (k). The wishes of the majority of the contributories will weigh with

(i) *Midland Counties Bank v. Attwood*
(1905) 1 Ch. 357.
(j) *Re Naokhali Loan Co.*, 51 C.W.N.

791.

(k) *Metropolitan Rly. Warehousing Co*
(1867) 17 L.T. 108.

the Court in this connection (l). If suspension is due to temporary causes, the Court will not order a winding up (m). Abandonment of some of the objects is not within the Cl., provided the principal object survives (n). A Co. cannot also be wound up under this cl. because it has amalgamated with another Co. and thus has ceased to carry on business. In such a case, the proper procedure is to move the Registrar under s. 569 to remove the Co.'s name from the Register as a defunct Co. (o).

Reduction of Members: As regards cl. (d), though the Court generally is averse to making an order for compulsory winding up on the ground that the membership of the Co. is reduced to below the permissible minimum but is generally inclined to leave the Co. to a voluntary winding up, it has been held in England that if the Court finds something wrong in the Co.'s affairs, it will order compulsory winding up under this cl. in suitable cases (p).

Inability to pay Debts: As regards cl. (e), "inability to pay debts", this is a cl. under which Co.s are most commonly sought to be compulsorily wound up. S. 434 lays down specific cases in which the Co. shall be deemed to be "unable to pay its debts". If any of them is proved, the Co. must be compulsorily wound up.

Statutory Notice: Cl. (a) of s. 434 refers to what is called a "statutory notice of demand". It may be compared with the "Insolvency notice" under the Insolvency Acts, which however refers to and is only confined to cases of judgment debts. The present cl. permits a statutory notice to be given in all cases of debts exceeding Rs. 500 by assignment or otherwise. The notice must fulfil all the requirements of s. 434(a), before it can be effective. A notice delivered at any other place than the registered office of the Co. would be invalid (q). When there is a *bona fide* dispute as to the Co.'s liability to pay the debt, the Court will not allow creditors of a Co. to invoke the assistance of the Companies Act for getting payment of their debt; they must be referred to a suit. Mere failure to comply with a statutory demand notice does not entitle the creditor to come before the Court in such a case and ask as a matter of right for the winding up of the Co. (r).

Inability to pay Debts: As regards cl. (c) of s. 434, if it is proved to the satisfaction of the Court that a Co. is unable to pay its debts, a compulsory winding up order would be justified. Whether in a given case, it is sufficiently proved that the Co. is unable to pay its debts, is a question of fact depending on the circumstances of each case. As was pointed out by the Patna High Court, in *Sudhaya Nath v. Bihar National Insurance* (s), when the Court is called upon to wind up a Co. on the ground that it is unable to pay its debts, what has to be ascertained is not whether the Co., if it converted all its assets into cash, will be able to discharge its debts, but whether, in a commercial sense, the Co. is solvent. In deciding whether a Co. is able to pay its debts, the uncalled capital of the Co. can be taken into account as available for the discharge of the Co.'s debts. The Court further observed that in determining whether a Co. should be wound up under this cl. the decisive question is whether at the date of the presentation of the petition there is any reasonable hope that the object of trading at a profit is attainable. The onus of proof lies on the petitioner. It is not the function of a judge in such a case to determine the question of the prospects of the Co. in future on its own views as to probable success or failure, but to form the best opinion it can upon evidence given by persons with practical knowledge of the trade in question and the local conditions when these affect the matter. Where, at the relevant time, there is a reasonable hope of tiding over a period of difficulty and emerging into a region where the Co. might reasonably expect to carry on at a profit, there is not sufficient reason for the winding up by Court under this cl. (t). Uncalled capital of a Co. is a valuable asset and has to be taken into consideration in deciding whether a Co. is unable to pay its debts and should therefore be wound up (u).

(l) *Ibid.*

(m) *Re Capital Firm Ins. Ass.* (1882) 21 Ch.D. 209.

(n) *Thellusone's Case* (1907) 2 Ch. 1.

(o) *National Financial Corp.* (1866) W.N. 243.

(p) *Re New Gas Co.*, 4 Ch.D. 874.

(q) *Bakıyarpur Light Rly. v. Union of India*, 93 C.L.J. 271.

(r) *Doraiswami v. Coimbatore Easswara etc. Ltd.*, A.I.R. (1929) Mad 265.

(s) 20 Pat. 538.

(t) *Ibid.*

(u) *Re National Live Stock Ins. Co.* (1858) 26 Beav. 152.

Just and Equitable: Cl. (f) of s. 433 is the most general cl. under which petitions for compulsory winding up of Co.s are usually made. The words "just and equitable" in the cl. are not to be construed "*ejusdem generis*" as only covering cases similar to those covered by the preceding cls. (v). As Kemp J. said in *In re Standard Aluminium and Brass Works (w)*, "the words 'just and equitable' are words of widest significance and do not limit the jurisdiction of the Court to any case. It is a question of fact and each case must depend on its own circumstances". The usual cases coming under the cl. are the following: (i) cases of deadlock, (ii) promotion of Co. for a fraudulent object, (iii) cases of oppression of minority by the majority, (iv) disappearance of substratum of Co., (v) lack of confidence in management, (vi) irregularities in the management of the Co.'s affairs.

Deadlock: Where there were two directors of a private Co., who were also the only shareholders, and they were not on speaking terms with each other, so that neither the board nor the "Co." (i.e. two directors) at general meeting could possibly conduct the business of the Co., Warrington L.J. ordered a compulsory winding up (x).

Fraudulent Object: Where the whole object of a Co. was fraudulent, e.g. to pass off the benefit of an old name to a newly started business in the same name as in *Brinsmead and Sons (y)*, the Court ordered a winding up. When object of the Co. was proved to be illegal, e.g. to conduct a lottery by means of creating prize fund by means of periodical contributions from members, *held*, the Court has jurisdiction under this cl. to wind up the Co. (z).

Oppression: The fact that one shareholder has preponderating influence is no ground for winding up (a). In *In re Cuthbert Cooper and Sons (b)*, in a private Co., the elder sons (who were the sole directors) of a deceased director, persistently refused to register the younger sons, on whom the part of their father's holding had devolved, as members, and also refused to give them copies of the balance sheet. *Held*, though the younger sons may have some right of action against their brothers, the above ground did not make it just and equitable that the Co. should be wound up.

Loss of Substratum: Cases of loss of substratum of a Co. are the following: where a Co. was formed for the purpose of acquiring a particular gold mine in New Zealand and title to it completely failed (c); where a Co. was formed to make coffee out of dates under a German patent and the patent could not be obtained (d). Where, however, the objects of a Co. as set out in the Memo. can be fulfilled by other ways or by employment of other agencies, it cannot be said that the substratum of the Co. is gone.

In a recent English case, a Co. was formed to acquire the undertakings of four other Co.s carrying on oil business in Russia. Before the undertakings could be acquired, they were confiscated by the then Russian Government and since a long time, the Co. had been engaged in attempting to substantiate their claim against the Russian Government. It had not otherwise carried on business and had considerable assets. *Held*, the substratum of the Co. has disappeared and it was just and equitable that the Co. should be wound up because such claim as the Co. had could be equally well enforced by the Liquidator (e).

Loss of Confidence: In *Lock v. John Blackwood Ltd. (f)*, a Co. was established as public Co. to carry on business of the testator and to divide profits in accordance with the terms of the will. When the petition for winding up had been presented, the directorate had held office for many years and had also preponderating voting power. The directors had, however, over a series of years, omitted to hold general meetings, to submit accounts or to recommend a dividend, and it was held by the Judicial Com-

(v) *Re New Bridge Sanitary Laundry Ltd.* (1907) 1 Ir.R. 67.

(w) 30 Bom. L.R. 1509.

(x) *Re Yenidje Tobacco Co. Ltd.* (1916) 2 Ch. 426.

(y) (1897) 1 Ch. 45.

(z) *Universal Mutual Aid Asso. v. Thappa Naidu*, 63 M.L.J. 554.

(a) *Rippon Press v. Gopal Chetty*, 58 I.A.

416.

(b) (1937) 2 All E.R. 466.

(c) *Re Havana Gold Mining Co.* (1882) 20 Ch.D. 151.

(d) *Re German Date Coffee Co.* (1882) 20 Ch.D. 159.

(e) *Baku Consolidated Oil Fields* (1944) 1 All E.R. 24.

(f) (1924) A.C. 783.

mittee that, in the circumstances, the confidence of the petitioning shareholders, not only in the policy, but also the probity of the directors, had been justifiably shaken and that they were entitled to the order prayed for.

Mismanagement: Whether "mismanagement" on the part of directors makes it "just and equitable" to wind up the Co. depends upon the facts of each case. As the Supreme Court pointed out in a recent case (*g*), where nothing more is established than that the directors have misappropriated the funds of the Co., an order for winding up would not be "just and equitable", because if it is a sound concern, such order must operate harshly on the right of the shareholders. But if, in addition to such misconduct, circumstances exist which render it desirable in the interests of the shareholders, that the Co. should be wound up, there is nothing in s. 162(6) which bars the jurisdiction of the Court to make such order. Where therefore it appeared that the Vice-Chairman of a Co. had grossly mismanaged the affairs of the Co. and had drawn considerable amount for his personal purposes, that there were substantial arrears due to Government for supplying electric energy, that large collections had to be made, that the machinery of the Co. was in a state of disrepair and that by reason of death or other causes, the directorate had become greatly attenuated and that a powerful local junta was "ruling the roost" and that the shareholders outside the group of the Chairman were apathetic and powerless to set the matter right, *held*, the Court had power to order that the Co. should be wound up.

Who may Petition

Under s. 439, cl. (i), an application to the Court for winding up a Co. shall be by petition presented either, (i) by the Co., or (ii) by any creditor or creditors including any contingent or prospective creditor or creditors, (iii) contributory or contributories, (iv) by all or any of those parties together or separately or (v) by the Registrar or (vi) by any person authorised by the Central Government under s. 243.

A contributory shall not be entitled to present a petition for winding up a Co. unless either (i) the number of members is reduced in case of a private Co. below two and in case of a public Co. below seven, or (ii) the shares in respect of which he is a contributory or some of them either were originally allotted to him or have been held by him and registered in his name, for at least six months during the eighteen months before the commencement of the winding up, or have devolved on him through the death of a former holder (cl. 4).

A contributory however shall be entitled to present a winding up petition notwithstanding that he is holder of fully paid-up shares and notwithstanding that the Co. may have no assets or surplus assets after satisfaction of liabilities (cl. 3). Further, a secured creditor is to be deemed to be a creditor of the Co. and so also a holder of debenture or debenture stock and the trustee for debenture-holder (cl. 2).

A petition for winding up a Co. on the ground of default in filing the statutory report or in holding the statutory meeting shall not be presented except by the Registrar or contributory nor before the expiration of fourteen days after the last day on which such statutory meeting ought to have been held (cl. 7). A petition for winding up by a contingent or prospective creditor shall not be admitted until leave of the Court for admission is obtained and such leave shall not be granted unless (i) such security for costs has been given as the Court thinks reasonable, and (ii) a *prima facie* case for winding up has been established to the satisfaction of the Court (cl. 8).

The Registrar shall not be entitled to present a winding up petition unless: (i) authorised to do so by the Central Government under s. 243 or (ii) unless the following grounds exist, viz. failure to hold statutory meeting or deliver statutory report, failure of Co. to commence business within a year from incorporation or suspension of business for one whole year or that the Co. is unable to pay its debts. In case of the last ground, the inability of the Co. to pay its debts must have appeared to him from the financial condition of the Co. as disclosed from the balance sheet or from the report of an Inspector appointed under s. 235 or 237 (see *ante*). In each of the above cases, how-

ever, the Registrar shall obtain the previous sanction of the Central Government before presenting the petition (cl. 5). The Central Government shall not accord such sanction until opportunity has been given to the Co. to make its representations (cl. 6).

Shareholder's Petition: An order for winding up can be made even when it is alleged that there are no assets, in order to provide machinery for ascertaining whether there cannot be shown to be assets (h). An order to wind up when there is nothing to wind up may at times be justified as a means of bringing to an end a vicious career (*Ibid.*). The fact that calls are unpaid does not debar a contributory from petitioning for winding up (i).

It was pointed out by Chagla J. in *Re Cine Industries, etc. Co. Ltd.* (j), a shareholder applying for an order for compulsory winding up of a Co. is under no obligation, to satisfy the Court that on a winding up there would be surplus assets. But in exercising its discretion to wind up a Co. on the petition of shareholder, the Court constantly bears in mind that the internal management of the Co. is its own affair and that it is a much better judge of the business prospects of the trading venture than the Court can ever hope to be. If therefore the majority of shareholders show confidence in the management of the Co. and have faith in its future prospects, the Court will rarely interfere. It is not right for a Court to intervene because one shareholder is dissatisfied. An applicant for winding up has got to make out a case for winding up on his petition. He cannot be allowed to fish out a case by cross-examination of the defendants who have made affidavits on behalf of the Co. or by inspecting the accounts.

Creditor's Petition: On a creditor's petition, the general rule is that the Court is bound to order a winding up, if the creditor fulfils the requirements of the sec., unless there are special reasons for doing otherwise (k). As between the creditor and the Co., who are his debtors, the unpaid creditor who shows insolvency, is entitled *ex debito justitiae* to a winding up order, that is to say, an order by virtue of which the creditor, by the hands of a liquidator, is entitled to seize the assets of the debtor and administer them for the payment of himself and all other creditors (l).

The order sought for by the petitioning creditor in such a case however is not an order for his own benefit, but is an order for the benefit of a class of which he is a member. The right *ex debito justitiae* is not his individual right but his representative right. If a majority of the class are opposed to his view and consider that they have a better chance of getting payment by abstaining from seizing the assets, then, upon general grounds and upon s. 91 of the Companies Act of 1862 (corresponding to s. 557 of the present Act), the Court gives effect to such right as the majority of the class desire to exercise (m).

Compulsory Winding up following Voluntary Winding up: Where a Co. is being wound up voluntarily or under supervision, a petition for winding up the Co. by the Court can be presented by (i) any person authorised under s. 439, subject to conditions prescribed therein (see *ante*) or (ii) by the Official Liquidator. The Court shall not make a compulsory winding up order on such petition unless it is satisfied that the voluntary winding up or winding up under supervision cannot be carried on with due regard to the interests of the contributories or creditors (s. 440).

The Court generally will not make a compulsory order in a case where a voluntary liquidation is pending on the petition of a creditor unless (i) the rights of creditors are injured or (ii) the general body of creditors desire it or (iii) the liquidator appointed is unfit. On a contributory's petition to the same effect, the Court will not make a compulsory order unless (i) the voluntary liquidation has been fraudulent or (ii) there are circumstances of suspicion or (iii) a searching investigation is needed. The Court has made such an order on a contributory's petition where it is supported by creditors

(h) *Krasnapolsky Restaurants etc. Co.* (1892) 1 Ch. 174.

(i) *Re Northern Airways Ltd.* (1947) C.C.L. 10.

(j) 44 Bom. L.R. 387.

(k) *Re Ilfracombe Building Society* (1901)

1 Ch. 103.

(l) *Crigglestone Coal Co.* (1906) 2 Ch. 327.

(m) *Crigglestone Coal Co.* (*supra*); *Ahmed Amin v. Dominion of India*, 54 C.W.N. 514.

and also to stop an unfair scheme of amalgamation being put through (n). The sec. is exhaustive of the persons entitled to apply thereunder. A Registrar therefore has *locus standi* to apply under the sec. Making of a compulsory order does not avoid *ab initio* all proceedings under a previous voluntary winding up (o).

Commencement of Winding up: When before the presentation of a petition for compulsory winding up, a resolution has been passed for voluntary winding up, the winding up shall be deemed to have commenced from the time of passing of the resolution. In all other cases, winding up shall be deemed to have commenced from the date of presentation of the petition. This sec. is new. It clarifies a point which was somewhat doubtful before. The position is now made clear by the present sec. The sec. provides that in case of winding up under supervision also, which is followed by a compulsory order, the date of presentation of petition shall be date of commencement of winding up (s. 441).

Powers of the Court

Interim stay of suits: Under s. 442, any time after presentation of petition and before making of a compulsory order any creditor or contributory or the Co. may apply for the stay of suits or proceedings pending against the Co. Such application must be made to the Supreme Court or the High Court if the suits or proceedings are pending therein. In all other cases, the application must be made to the Court having jurisdiction to wind up the Co. The respective Court may stay or restrain the proceedings on such terms as they think fit. Before granting stay, the Court may require the Co. to give security (p).

Hearing of Petition: At the hearing of a petition, the Court may (a) dismiss it with or without costs, (b) adjourn it conditionally, (c) make any interim order it may think fit or (d) make a *winding up order with or without costs or make any other order that it thinks fit*. The Court however shall not refuse to make a winding up order on the ground that the Co.'s assets are mortgaged to an amount equal to or in excess of the assets or that it has no assets. When a petition is presented on the ground that it is "just and equitable" that the Co. shall be wound up, the Court may refuse to make up a winding up order, if in its opinion there is another remedy open to the petitioners and that they are acting unreasonably in asking for a winding up, instead of pursuing that remedy. Further, when the petition is presented on the ground of failure to hold statutory meeting or deliver the Statutory Report, *the Court may direct that the Report be delivered or the meeting be held* and may also make proper order as to costs (s. 443).

Proceedings after Winding up Order: Under s. 444, on making a winding up order, the Court shall forthwith cause intimation thereof to be sent to the Off. Liquidator. The petitioner as well as the Co. also under s. 445 are bound, within one month of the making the order to file a certified copy of the order with the Registrar. If default is made in this behalf, the petitioner, the Co. and every officer in default shall be liable to a fine. The Registrar, on the order being filed with him, shall make a minute thereof in his books relating to the Co. and shall notify the order in the Off. Gazette. An order of winding up shall be deemed to be notice of discharge to the officers and employees of the Co. except when the business of the Co. is continued. Under s. 447 the winding up order operates in favour of all the creditors and contributories of the Co. as if made on the joint petition of a contributory and a creditor. Order of winding up relates back to the date of the petition. Transactions subsequent to that date are not binding on the liquidator, except with specific sanction of the Court (q).

Stay of Suits and Proceedings: When a winding up order is made or the Off. Liq. has been appointed provisional liquidator, no suit or legal proceedings shall be commenced or if pending at the date of the order, shall be proceeded with, against the Co. except by leave of Court and subject to terms it may impose. Notwithstanding any law to the contrary, the winding up Court shall have jurisdiction to entertain or dispose off

(n) Consolidated South Rand Mines
(1909) 1 Ch. 491.

(o) Thomas v. Patent Leonite Co. (1881)
17 Ch.D. 250.

(p) Virbhajji v. Wadia Mills, 18 Bom. 65.

(q) H. Naik v. Penclanan Das, A.I.R.
(1952) Cut. 309.

any suit or proceeding by or against the Co. Pending suits or proceedings by or against the Co. may, in spite of any provision of law to the contrary, be transferred to and disposed off by the winding up Court. Under the present sec., the winding up Court has jurisdiction to dispose off all pending suits and proceedings by or against the Co. and the same may therefore be transferred to the winding up Court by the other courts where they are pending for the purpose of disposal (s. 446).

POWERS OF COURT AND LIQUIDATOR IN COMPULSORY WINDING UP

Official Liquidators: The present Act makes a salutary departure by providing in s. 448, that for purpose of winding up, there shall be attached to each High Court an Official Liquidator appointed by the Central Government, who may be either a whole-time or part-time officer as the exigencies of the case may require. As regards District Courts, the Official Receiver and if there is none such, an appointee of the Central Government shall be the Official Liquidator. The appointment of Official Liquidator as Liquidator of the Co. on a winding up order being made is automatic (s. 449). The Official Liquidator can, under s. 450, if the Court thinks fit, be also appointed provisional Liquidator on a winding up petition being presented and before winding up order is made.

Powers of Provisional Liquidator: Before appointing the Official Liquidator as provisional liquidator, notice must be given to the Co. and a reasonable opportunity must be given to it to make representation, unless for special reasons to be recorded, such notice is dispensed with. The provisional liquidator shall have the same powers as the Official Liquidator unless the Court, by the order appointing him or by a subsequent order, limits his powers. On a winding up order being made, he shall automatically become the liquidator of the Co. (s. 450).

Duties of Liquidator: Generally, the Liq. of a Co. in compulsory winding up must conduct the winding up and perform such duties in reference thereto as the Court may impose. When the Official Liq. is appointed Liq., such fees shall be paid to the Central Govt., out of the assets, as may be prescribed (s. 451). A Liq. shall be styled as "the Official Liquidator" of a particular Co. and not by his personal name (s. 452). No receiver can be appointed of assets in the hands of the Liq., except by or with the leave of the Court (s. 453). Disturbance of possession of the Liq. amounts to a contempt of Court (r). Even a secured creditor cannot disturb his possession without leave of the Court (s).

Position of Liquidator: The Liq. occupies a double position in winding up. He represents the Co. and he also represents the creditors of the Co. The result is that he must assert rights against the Co. and further, he can assume against the members of the Co., a position which the Co., if solvent, could not itself have taken up (t).

Statement to be made to Official Liquidator: S. 454 provides that when a winding up order has been made or the Official Liquidator is appointed provisional Liquidator, a statement of the affairs of the Co. in prescribed form, verified by an affidavit shall (unless dispensed with by Court) be submitted to him containing following particulars: (a) assets of the Co. distinguishing cash balance in hand and at the Bank and negotiable securities (if any) held by Co., (b) its debts and liabilities, (c) names, residences and occupations of its creditors, distinguishing amount of secured and unsecured debts, and in the former case, the securities given, *whether by the Co. or an officer thereof*, their value and their dates, (d) debts due to Co. with names, residences and occupations of persons from whom they are due and the amount likely to be realised, and (e) such further information as may be prescribed or *the Official Liq. may require*. The statement must be submitted and verified by one or more of the persons who are directors at the relevant date and by a person who at such date is manager, secretary or chief officer of the Co. or by such of the following persons as the Official Liq. may, subject to sanction of Court, require, viz. (a) present or ex-officers of the Co.; (b) persons who have taken part in the formation of the Co. within 1 year of the "relevant date"; (c)

(r) Re Pound (1889) 42 Ch.D. 402.

(s) Ibid.

(t) Waterhouse v. Jamaison, L.R. 2 H.L. 29.

present employees or persons who have been employees of the Co. within the said year and who in the Off. Liq.'s opinion are capable of giving the required information; and (d) persons who are or have been within the said year officers in employment of a Co., which is or which was, within the said year, an officer of the Co. in liquidation. The statement must be submitted within 21 days of the appointment of the provisional Liq. or in absence of such appointment, within 21 days of the winding up order (those two being the "relevant dates" under the sec.). The period may be extended for special reasons by the Off. Liq. or the Court to not more than 3 months. Reasonable costs for preparing such statement must be paid to the person preparing the same. Failure without reasonable cause to comply with the above requirements is punishable with fine. Persons claiming in writing to be creditors or contributories of the Co. are entitled to inspect the statement at reasonable times on payment of prescribed fees. Falsely claiming to be creditor or contributory is an offence under s 182, I.P.C., punishable on complaint of Off. Liq.

Report by Official Liquidator: Under s. 455, the Off. Liq. shall, as soon as practicable after receipt of statement under s. 454 *but not more than 6 months from the date of winding up order*, and when statement is dispensed with, as soon as practicable after the winding up order, submit a preliminary report to the Court, stating: (a) the amount of capital issued, subscribed and paid up, estimated amount of assets and liabilities with separate particulars of (i) cash and negotiable securities, (ii) debts due from contributories, (iii) debts due to Co. and securities therefor, (iv) movable and immovable properties of the Co., and (v) unpaid calls; (b) if the Co. has failed, the cause of such failure; (c) whether in his opinion further inquiry is desirable with regard to promotion, formation or failure of Co. and the conduct of the business thereof. The Off. Liq. may also make further and other reports also, as regards the manner in which the business of the Co. has been conducted, whether any fraud has been committed by any person in promotion or formation of the Co. or by any officer in relation to the Co. and all other matters which may be required to be brought to the Court's notice. If in any further report the Off. Liq. states that in his opinion a fraud has been committed as aforesaid, he shall have further powers under s. 478, e.g. to apply for public examination of directors and other persons connected with the Co.

Powers of Liquidator

S. 457 divides the powers of a Liq. into two classes: (i) those which can be exercised by him only with the sanction of the Court and (ii) those which do not require such sanction for their exercise. The following powers require sanction of the Court: (a) to institute and defend suits, prosecutions and other legal proceedings, civil or criminal, in the name of and on behalf of the Co., (b) to carry on business of the Co. for its beneficial winding up, (c) to sell immovable and movable property and actionable claims belonging to the Co. by public or private sale, with power to execute necessary transfers, (d) to raise money on security of the Co.'s property, and (e) to do all other acts as may be necessary to wind up the Co. and to distribute its assets.

The following powers do not require sanction of the Court for their exercise: (i) to do acts and execute in the name of the Co. and on behalf of the Co., all deeds, documents, etc., and to use the Co.'s seal where necessary; (ii) to prove, rank and claim in the insolvency of any contributory and to receive dividends out of his estate; (iii) to draw, accept, make and endorse, bill of exchange, hundi, or pro-note in the name of and on behalf of the Co.; (iv) to take out in his official name, letters of administration to any deceased contributory and in his official name to do all things necessary for obtaining any money from a contributory or his estate, as if the moneys were due to himself (but not so as to affect the powers of the Administrator-General); (v) to appoint agents where necessary. The exercise of the above powers is subject to the control of the Court and any creditor or contributory can apply to the Court with respect to the exercise or proposed exercise of the same. Under s. 458, the Court may, by order, provide that any of the powers mentioned in the first part, may be exercised by the Liq. without the sanction of the Court, provided that such exercise shall be subject to the control of the Court. Under s. 459, the Liq., with the sanction of the Court, may appoint an advocate, attorney or pleader to appear before the Court to assist him in the performance of his duties.

Power to compromise: S. 456 gives power to Liq. in compulsory winding up, *inter alia*, to enter into compromises with the sanction of the Court. Under the sec., in case of winding up by the Court, the Liq., with the sanction of the Court, may (i) pay any class of creditors in full, (ii) make any compromise or arrangement with creditors and alleged creditors, claimants and alleged claimants (whether present or future, certain or contingent, ascertained or sounding in damages), against the Co., and (iii) compromise any call, or liability to call, debt or liability capable of resulting in debt, any claim (present, future, certain, contingent, ascertained or sounding only in damages), between the Co. and a contributory or debtor and all questions affecting assets or liabilities of the Co. being wound up, on such terms as may be agreed and take such security for discharge of the same and give complete discharge in respect of the same. Any creditor or contributory may apply to Court with regard to the exercise or proposed exercise of such power. A Liq. with the sanction of the Court has power to compromise a claim (u). It has been held by a Full Bench of the Lahore High Court in case of a voluntary liquidation, that the Liq. has no power to refer a dispute to arbitration (v).

Disclosure of fact of Liquidation: Where a Co. is being wound up by Court, every invoice, order for goods and business letter issued by or on behalf of the Co., Liq., manager or receiver and bearing the Co.'s name, shall also state that the Co. is being wound up. Default in compliance with the above is punishable by a fine for Co. and for officer, liquidator, receiver or manager, who wilfully authorises the same (s. 547). Where winding up is not concluded within a year after its commencement, the Liq. within one month of conclusion of such year and thereafter till conclusion of winding up, at intervals of not more than one year (or such shorter period as may be prescribed) file in Court a statement in prescribed form with prescribed particulars as to the position of the liquidation. A copy of the statement shall also be simultaneously filed with the Registrar. Any person claiming in writing to be a creditor or contributory of the Co. shall be entitled to inspect the same on payment of a small fee. Failure to comply with the sec. is punishable with fine for the Liq. Falsely claiming to be creditor or contributory is punishable as an offence under s. 182 of the Indian Penal Code (s. 551).

Payment into Public Account: Every Off. Liq. shall pay moneys received by him as such into the public account of India in the Reserve Bank in such manner and at such times as may be prescribed. No Off. Liq. or any other Liq. of a Co. shall pay moneys received by him as such into any private banking account (s. 552).

Control over Acts of Liquidator: The Liq., subject to the provisions of the Act, is bound to have regard in administration of the Co.'s assets and the distribution thereof, to the directions given by resolutions of general meetings of creditors or contributories or by the committee of inspection. Any directions given by creditors or contributories at general meeting, shall be deemed to override any given by the committee of inspection, in case of conflict. The Liq. can summon general meetings of creditors and contributories whenever he thinks fit to ascertain their wishes. He shall be bound to summon such meetings, when called upon to do so by meetings of creditors or contributories or when requested in writing by 1/10th in value of the creditors or contributories (s. 460). The Liq. may apply to the Court in prescribed manner for directions in respect of any matter relating to winding up. Any person aggrieved by any act or decision of the Liq. may apply to the Court and the Court may confirm, reverse or modify the act or decision complained of and may make such further order as in the circumstances it thinks just. In such appeals it has been held that the Liq. cannot take sides but must be completely impartial (w). Subject to the provisions of the Act, the Liq. is entitled to use his own discretion in the administration of the Co.'s assets and the distribution thereof among the creditors. The Court is now given power, on application of a contributory creditor or the Registrar to order the Liq. within 14 days of service of notice on him, to make good any default on his part in filing, delivering or making any return, account or other document which by law he is required to file, deliver, make or give. The costs

(u) Bank of Hindustan v. Eastern Financial Ass., 13 M.I.A. 15.

(v) Dunichand v. Naraindas (1947) Lah.

355.

(w) Rippon Press v. Gopal Chetty, 58 I.A. 416.

of all parties on such application may be thrown on the Liq. Penalty imposed on Liq. by other laws is not affected by the above (s. 556).

Committee of Inspection

Within 2 months of the winding up order, the Liq. shall convene a meeting of creditors of the Co. (as ascertained from the books, documents, etc. of the Co.) for determining whether a Committee of Inspection should be appointed with the Liq. and who shall be its members. Within 14 days (or such further time as the Court may allow) of such meeting, the Liq. shall convene a meeting of contributories to consider the decision of the creditors' meeting. Such meeting may accept or reject the said decision or accept it with modification. Unless the contributories' meeting accepts the decision of the creditors' meeting, it shall be the duty of the Liq. to apply to the Court for directions as to whether there shall be such Committee and if so, who shall be its members (s. 464). The Committee shall consist of not more than 12 members, being creditors and contributories of the Co. or persons holding general power of attorney from them, in such proportions as may be agreed upon by them at their meetings and in case of disagreement, as decided by the Court. The Committee shall have right to examine the Liq.'s accounts at all reasonable times. It shall meet at fixed agreed times and failing same, at least once a month. The Liq. or any member of the Committee may also call a meeting. *The quorum shall be 1/3rd of the total number of members or two, whichever is higher.* The Committee shall act by majority of members present but shall not act unless the quorum is present. A member may resign by notice in writing signed by him, and delivered to the Liq. If a member is adjudged insolvent or compounds with creditors or is absent at 5 consecutive meetings without the consent of his fellow members, his office shall become vacant. A member may be removed also at a meeting of his class members by ordinary resolution after 7 days' notice, stating its object. On a vacancy arising, the Liq. shall forthwith call a meeting of the class of the ex-member. Such meeting can, by ordinary resolution, appoint the same member or any other creditor or contributory to fill the vacancy. If the liquidator having regard to the state of winding up, is of opinion that the vacancy need not be filled, he shall apply to the Court and the Court may order that such vacancy shall not be filled or shall be filled in certain circumstances. Continuing members of the Committee may continue to act notwithstanding the vacancy (s. 465).

General Powers of Court in Compulsory Winding up

(i) **Power to stay winding up proceedings:** The Court may, at any time, after making a winding up order, on the application of Off. Liq. or a creditor or contributory and on proof that all further proceedings in winding up should be stayed, make a stay order accordingly, either altogether or for a limited time and on such terms as the Court thinks fit; the Court before making a stay order may require the Off. Liq. to furnish the Court with a report on all relevant matters. A copy of the order under the sec. shall be forthwith forwarded to the Registrar by the Co. or other prescribed persons and the Registrar shall make a minute of the order in his books (s. 466).

(ii) **Settlement of List of Contributories:** As soon as possible after making a winding up order, the Court shall settle a list of contributories, and shall cause the assets to be collected and applied in discharge of the Co.'s liabilities. For the purpose of settling the list of contributories the Court shall have power to rectify the Register when the same is required in pursuance of the Act. No list of contributories need be settled where it appears to the Court that no calls would have to be made or adjustment of rights of contributories will be necessary. In making the list the Court shall distinguish between those who are contributories in their own right and those who are contributories as representatives of or liable for the debts of others (s. 467).

The liability of a member to be included in the list of contributories is 'ex legis' and not 'ex contractu'. A member who objects to his name remaining on the Register on any ground should promptly take steps to have the register rectified. If he fails

to do so and winding up supervenes he will be liable as contributory and estopped from denying the same (x).

(iii) **Delivery of Property:** The Court may at any time after making a winding up order, require any contributory, for the time being on the list of contributories, any trustee, receiver, banker, agent or officer of the Co., to pay, deliver, surrender or transfer to the Liq. forthwith within time fixed by Court any money, property, books and papers in his hands, to which the Co. is *prima facie* entitled (s. 468).

(iv) **Payment of debt due by Contributory and extent of Set-off:** S. 469 provides that the Court may, after a winding up order has been made, make an order on any contributory for the time being on the list, to pay as directed, any money due to the Co. by him or by the estate he represents, exclusive of any money, payable by him or by the estate he represents, by virtue of any call made in pursuance of the Act (for which see *seq.*). The Court may, in making such order, allow to such person a set-off: (i) in case of unlimited Co., of money due by the Co. to him or to the estate he represents on any independent dealing or contract with the Co. but not in respect of any money due for dividend or profit, (ii) make a like allowance in case of a director, managing agent, secretaries and treasurers or manager of a limited Co., whose liability is unlimited, and (iii) in case of a Co., whether limited or unlimited, after all creditors have been paid in full, allow against a subsequent call any money, due to such person, on any account whatever. The sec. gives a summary power to the Court to direct any contributory to pay up any debt due by him to the Co. otherwise than for call. No set-off is to be allowed to him in such a case, except in the three cases mentioned above, subject to the conditions therein mentioned. The inclusion of managing agents, secretaries and treasurers and manager, with unlimited liability, is new.

As pointed out by Lord Russel of Killowan in *Hansraj Gupta v. Official Liquidator of Dehra Dun, etc. Tramways Co. Ltd.* (y), however, three features of the sec. are to be noted: (1) It is only concerned with moneys due from a contributory other than moneys payable by virtue of a call in pursuance of the Act. A debtor who is not a contributory is untouched by it. Money due from him is recoverable only by suit in the Co.'s name. (2) It is a sec. which creates a special procedure for obtaining payment of money; it is not a sec. which purports to erect a foundation upon which to base a claim for payment. It creates no new rights. (3) The power of the Court to order payment is discretionary. It may refuse to act under the sec., leaving the Liq. to sue in the name of the Co. and it will readily take that course in any case in which it is made apparent that the respondent under the procedure, if continued, would be deprived of some defence or answer open to him in a suit for the same moneys.

(v) **Power to make calls:** Any time after a winding up order has been made and either before or after the sufficiency of the Co.'s assets has been ascertained, the Court may, at any time, make calls on all or any of the contributories on the list, to the extent of their liability, for payment of any money which the Court considers necessary to satisfy the debts and liabilities of the Co., the costs, charges and expenses of winding up and for adjustment of the rights of contributories among themselves and may also make an order for payment of such calls. In making a call, the Court may take into consideration the probability that some contributories may fail to pay the same, wholly or partly (s. 470). An order under the sec. is called a "balance order". It is executable as a decree (z). No set off is allowed to a contributory as regards any debt due by the Co. to the contributory as against call moneys due from same to the Co. There is no difference in the rule whether the call is made before or after winding up (a). The only exception is where a contributory is himself bankrupt (see *seq.*).

(vi) **Payment Order:** The winding up Court may order "any contributory, purchaser or other person from whom any money is due to the Co." to pay the money into the Public Account of India in the Reserve Bank instead of the Liq. The order can be enforced in the same manner as if it directed payment to the Liq. (s. 471). All

(x) *Laxmi Narsi Reddi v. Off. Liq.* (1952) 1 M.L.J. 488.

(y) (1933) A.L.J. 175.

(z) *Praduman Sing v. Pioneer Jewellery Co.*, 67 I.C. 443.

(a) *Barnett's Case* (1873) L.R. 19 Eq. 449.

moneys, bills, hundis, notes and other securities paid or delivered into the Reserve Bank in the course of a compulsory winding up shall be subject in all respects to the order of the Court (s. 472). An order made by the Court on a contributory shall, subject to any right of appeal, be conclusive evidence that the money thereby appearing to be due or ordered to be paid is due. All pertinent matters stated in such an order shall also be taken as truly stated as against all persons and in all proceedings whatsoever (s. 473). A contributory dissatisfied with a "balance order" can only appeal against the same under s. 483. Procedure by way of suit to recover calls is not barred.

(vii) Time Limit for Proof of Debts and Claims: The winding up Court shall fix the time or times within which creditors are to prove their claims or be excluded from the benefit of any distribution made before such debts or claims are proved (s. 474). One of the main duties of a Liq. is to ascertain the debts due or claims outstanding against the Co. and to pay them off or otherwise settle with the parties concerned with the sanction of the Court (see s. 546). For the above purpose he has to invite claims and require them to be proved before him. Proof is lodged by means of affidavits stating full particulars of the claim and mentioning the evidence by which they are supported. The Liq. on examining such proofs may admit them wholly or in part or reject them. A time-limit is required to be fixed by the sec. for creditors and claimants to lodge proof of their claims. If such proof is not lodged within the prescribed time-limit, the creditor or claimant shall have no right to disturb a dividend already declared or payment already made (b). He however is not prevented by the sec. from participating in any distribution made after his proof is lodged. A creditor can prove his claim so long as any assets of the Co. remain undistributed in the hands of the Liq. (c). For detailed consideration as regards debts provable see *seq.*

(viii) Right of Private Examination: S. 477 provides that the Court may, at any time after the appointment of a provisional liquidator or the making of a winding up order, summon before it (i) any officer of the Co. or (ii) any person known or suspected to have in his possession any property or books or papers of the Co. or (iii) known or suspected to be indebted to the Co.; or (iv) any person whom the Court deems capable of giving information concerning the promotion, formation, trade dealings, property, books or papers or affairs of the Co. The person summoned may be examined by the Court on oath by word of mouth or by written interrogatories. In the first case, his answers may be taken down in writing and he may be asked to sign the same. He may be required to produce any books or papers relating to the Co. in his custody or power. If he claims a lien on the same, he shall produce them without prejudice to the lien and the winding up Court shall have jurisdiction to decide all questions regarding such lien. If such person, after being offered reasonable sum for expenses, fails to appear before the Court (not having a lawful impediment made known to and allowed by the Court), he can be apprehended and brought before the Court for examination.

(ix) Power to order Public Examination: S. 478 provides that (i) when a winding up order is made and the Off. Liq. has made a report to the Court under the Act, stating that in his opinion a fraud has been committed by any person in the promotion or formation of the Co. or by an officer of the Co. in relation to the Co. since its formation, the Court may, after considering the report, direct that such person or officer shall appear before the Court on an appointed day and be publicly examined as to the promotion or formation or the conduct of the business of the Co. or as to his own conduct and dealings as an officer of the Co. (ii) The Off. Liq. shall take part in the examination and may, if specially authorised, employ such legal assistance as may be sanctioned by the Court. (iii) A creditor or contributory may also take part in the examination either personally or by qualified advocate or attorney. (iv) The Court may put such questions to the person examined as it thinks fit. (v) The person in question shall be examined on oath and shall be bound to answer all questions put or allowed to be put to him. (vi) Such person, before his examination, shall be furnished at his own cost with a copy of the Report of the Off. Liq. and he may at his own cost employ a qualified advocate, attorney or pleader who shall be at liberty to put such questions to him as the Court thinks fit for explaining or qualifying any answers given by such person. (vii) If such person

(b) *Hicks v. May*, 13 Ch.D. 236.

(c) *Re McMurdo* (1902) 2 Ch. 684; *Raj-*

kumari v. Motion Pictures Combine Ltd., A.I.R. (1942) Mad. 349.

applies to the Court to be exculpated from any charge made or suggested against him, it shall be the duty of the Off. Liq. to appear at the hearing of such application and call the attention of the Court to all relevant matters. The Court after hearing the evidence given or witnesses called by the Off. Liq. may allow such application and in that event allow the applicant such costs as it thinks fit. (viii) Notes of the examination shall be written down and shall be read over to the person examined and be signed by him. They may thereafter be used in evidence against him and shall be open to inspection of any creditor or contributory at all reasonable times. (ix) The examination may be adjourned from time to time. (x) An examination under the sec. can be held before any District Judge or before any officer of the High Court (being an Official Referee, Master, Registrar or Deputy Registrar), if the Court directs and subject to any rules in that behalf. (xi) The powers of the Court under the sec. as to the conduct of the examination, but not as to costs, shall apply to such examination. As distinguished from s. 477, the present sec. deals with what is called the "public examination" of directors and other officers of the Co. who have been connected with the formation of the Co. and with the conduct of its affairs.

Dissolution of Company: After the affairs of the Co. are completely wound up the Court shall make an order that the Co. shall be dissolved from the date of the order and the Co. shall be dissolved accordingly. Within 14 days of the order, a copy thereof shall be forwarded by the Liq. to the Registrar who shall enter the minutes thereof in his books. Penalty for default on part of Liq. is a fine (s. 481). On dissolution, a Co. ceases to exist and its corporate existence comes to an end (d). A solicitor filing or defending a suit on behalf of a dissolved Co. may have to pay the opponent's costs personally (*Ibid*). All property and assets belonging to the Co. at the time of its dissolution, in absence of any other disposal thereof, become "bona vacantia" and vest in the Crown (e). Under s. 559, the Court has power to declare a dissolution void, on proper application being made for the purpose by the proper person (see *seq.*).

VOLUNTARY WINDING UP

Voluntary Winding up Generally: Of all forms of winding up an incorporated Co. voluntary winding up is by far the most common and the most popular form. This is because of the facilities it provides to both the shareholders and the creditors of a Co. to sit together and by evolving a domestic forum, to put an end to the difficulties and disputes which may have arisen in connection with the running of the Co.'s business. An unregistered Co. cannot be wound up voluntarily under the Act (see s. 583), but such Co.s can register themselves under Part IX of the Act and then wind up voluntarily.

When Co. can be wound up voluntarily: A Co. may be wound up voluntarily (a) when the period (if any) fixed for the duration of the Co. by the articles has expired or the event (if any) has occurred on the occurrence of which the articles provide that the Co. should be dissolved and the Co. in general meeting passes a resolution for voluntary winding up; (b) if the Co. passes a special resolution that the Co. be wound up voluntarily. A "resolution for voluntary winding up" under the Act means a resolution passed under cl. (a) or (b) above (s. 484). Where a voluntary winding up is desired, care must be taken to see that proper notices are given of the relevant resolutions intended to be passed. If the notices are defective, the resolution for "winding up" and the winding up which follows will both be bad (f). A Co. can be voluntarily wound up by an ordinary resolution only if it is bound to cease functioning at a certain time under its articles. It can be wound up voluntarily by special resolution for any reason.

The Co. after passing a resolution for voluntary winding up, must within 14 days thereof advertise the same in the Official Gazette and in some newspaper circulating in the district in which the registered office of the Co. is situate. In case of default, the Co. and every officer (which includes the Liq. also) in default, are both liable to a fine (s. 485).

(d) *Salton v. New Beeton Cycle Co.*
(1900) 1 Ch. 43.

(e) *Re Wells* (1932) 1 Ch. 380.

(f) *Manchester Economic Building Society*
(1883) Ch.D. 488; *Ramprasad v. Union*
Bank of India, 35 P.R. 1917.

Commencement of Voluntary Winding up: A voluntary winding up shall be deemed to commence at the time when the resolution for voluntary winding up is passed (s. 486). Where after a resolution for voluntary winding up has been passed, a petition is presented to the Court for compulsory winding up, on which a compulsory order is made, s. 441 now provides that the winding up shall be deemed to have commenced from the time the resolution for voluntary winding up was passed and unless on proof of fraud or mistake the Court otherwise directs, all proceedings taken in the voluntary winding up shall be deemed to have been validly taken. The sec. has the effect of clarifying a point on which there was formerly a difference of opinion in India as well as in England.

Consequences of Voluntary Winding up: In case of voluntary winding up, from the commencement thereof, the Co. shall cease to carry on its business except so far as may be required for its beneficial winding up. The corporate state and the corporate powers of the Co., however, shall continue until it is dissolved (s. 487)

Declaration of Solvency

S. 488 provides that (i) where it is proposed to wind up a Co. voluntarily, the directors or a majority of them (where they are more than two) may, at a meeting of the Board, make a declaration verified by affidavit to the effect that they have made full inquiry into the affairs of the Co. and that having done so, have formed the opinion that the Co. *has no debts* or that it will be able to pay its debts in full within a period not exceeding three years from the commencement of winding up as may be specified in the declaration. (ii) Such declaration shall have no effect for purposes of the Act unless (a) it is made within the five weeks immediately preceding the date of the passing of the resolution for winding up and is delivered to the Registrar before that date and (b) it embodies a statement of the Co.'s assets and liabilities as at the latest practicable date before the making of the declaration. (iii) A director making such declaration without having reasonable grounds for the opinion therein expressed (as to the Co.'s ability to pay its debts) is punishable with imprisonment (upto 6 months) or fine (upto Rs. 5,000) or both. (iv) If the Co. is wound up (voluntarily) in pursuance of a resolution passed within the period of five weeks after the making of the declaration and the debts of the Co. are not paid or provided for within the period specified in the declaration, it shall be presumed that the Director had no reasonable grounds for his opinion. (v) Where such a declaration is duly made and delivered, the winding up following shall be called "members' voluntary winding up". Where the same is not duly made or delivered, it shall be called "creditors' voluntary winding up". The purpose of the declaration is to notify that in the reasonable opinion of the directors, the Co. is a solvent Co., so that its winding up can be safely left in the hands of the shareholders as distinguished from its creditors who would be the principal parties concerned if the Co. was unable to pay its debts within a reasonable period of time after commencement of winding up. Directors making such declaration do not thereby stand guarantee for the payment of the Co.'s debts within the period specified, but as cl. (iv) states, the burden of proving that they had reasonable grounds for forming their opinion that the Co. would be able to pay its debts, would be on them, if ultimately the said debts are not paid within the specified period. If the declaration is made without reasonable grounds for making the same the directors are liable to be prosecuted under cl. (iii).

Members' Voluntary Winding up

(i) **Appointment of Liquidator:** The Co. in general meeting shall appoint one or more Liq.s for winding up the affairs of the Co. and for distributing its assets. The Co. in general meeting shall also fix the remuneration payable to the Liq.s. (ii) Any remuneration so fixed shall not be increased in any circumstances whatever with or without the sanction of the Court. (iii) Before such remuneration is fixed, the Liq. or Liq.s shall not take charge of the Co.'s assets. (ii) On the appointment of Liq. all powers of the Board and of *managing or whole-time director, managing agents, secretaries and treasurers and manager (if any)* shall cease, *except for purposes of giving notice to Registrar under s. 493 (see seq.)* or in so far as the Co. in general meeting or the Liq. sanctions their continuance (s. 491). (iii) A vacancy in office of Liq. caused by

except so far as the Committee of Inspection (if any) or the creditors in general meeting sanction their continuance (s. 505). (vii) *Vacancy*: If vacancy occurs by death, resignation or otherwise in the office of Liq. (except one appointed by or under the directions of the Court), the creditors in general meeting may fill the vacancy (s. 506).

(viii) *Amalgamation*: The Liq. in a creditors' voluntary winding up has, under s. 507, the same powers to accept shares, etc. of a transferee Co. as a Liq. in a members' voluntary winding up has under s. 494, except that the powers in his case, shall not be exercised by him except with the sanction of the Committee of Inspection or the Court (s. 507).

(ix) *Meeting at end of each year*: If the winding up continues for more than a year, the Liq. shall call a general meeting of the Co. and a meeting of the creditors at the end of the first year after commencement of winding up and at the end of each succeeding year or as soon thereafter as convenient *within 3 months of end of each year or such longer time as the Central Government may allow* and lay before the meetings an account of his acts and dealings and the conduct of the winding up during preceding year, with a statement in the prescribed form, containing prescribed particulars with regard to the position of the winding up. The penalty for failure is a fine (s. 508). (x) As soon as the Co.'s affairs are wound up, the Liq. shall make up the account of the winding up showing how the winding up has been conducted, how the Co.'s property has been disposed off and call a general meeting of the Co. and a meeting of creditors laying the account before them and explaining the same to them. On failure, the Liq. is liable to a fine. Each meeting shall be called by advertisement specifying the time, place and object thereof, and published in the Official Gazette and also in some newspaper circulating in the district where the registered office of the Co. is situate. Within one week of the meetings or the last meeting, if the meetings are not held on the same day, the Liq. shall send a copy of the account to the Registrar as also a return of the holding of the meetings, and the date or dates hereof. On default Liq. is liable to fine. If a quorum (which shall not be less than two) is not present at either of the meetings, the Liq. shall instead of the above return, make a return stating the said fact. On receiving the above account and either of the above returns, the Registrar shall forthwith register them and on expiration of 3 months from such registration the Co. shall be deemed to be dissolved, provided that on the application of the Liq. or any other person who appears to the Court to be interested, the Court may defer the time for dissolution to such period as it may think fit. The person on whose application, such order deferring dissolution has been made shall within 21 days of the date thereof, deliver to the Registrar a certified copy of the order for registration. Failure is punishable with fine (s. 509).

PROVISIONS APPLICABLE TO BOTH KINDS OF VOLUNTARY WINDING UP

Distribution of Property: Subject to the provisions of the Act as regards preferential payments, the assets of the Co. in winding up shall be applied in satisfaction of all its liabilities *pari passu* and shall, subject thereto, be distributed, unless the articles otherwise provide, among members according to their rights and interests in the Co. (s. 511). The sec. requires all debts and liabilities to be discharged *pari passu*, except as regards debts which are made preferential by Statute. One result of this rule is that no ordinary creditor will be allowed to steal a march over other such creditors by obtaining a decree and levying execution. A voluntary winding up does not operate as an automatic stay of suit as in case of compulsory winding up under s. 446. It is the usual practice of the Courts in England, however, to grant a stay of execution when the Co. has gone into voluntary liquidation (g).

Powers of Liquidator in Voluntary Winding up: Under s. 512, the Liq. may: (a) in case of members' voluntary winding up with the sanction of special resolution of the Co. and in case of creditors' voluntary winding up with the sanction of the Court or the Committee of Inspection and in absence of the last, of a meeting of creditors, exercise powers given by s. 457(2), cls. 1-4, to Liq. in compulsory winding up, i.e. (i) to do all acts and execute all documents on behalf of Co., (ii) to prove in insolvency of a contri-

butory, (iii) to draw, accept, endorse, Bill of Exchange, Hundi or promissory note on behalf of Co., (iv) to take out letters of administration to estate of a deceased contributory and to take all necessary steps to recover moneys due from a contributory, (v) and to do all other things as may be necessary for winding up the Co. and distributing its assets. The exercise of these powers shall be subject to control of the Court, and any creditor or contributory may apply to Court in respect of exercise or proposed exercise of any of the powers; (b) without such sanction, exercise all other powers given under the Act to the Liq. in case of winding up by the Court, (c) exercise the powers of the Court under the Act for settling list of contributories (which shall be *prima facie* evidence of liability of the persons named as contributories), (d) exercise power of Court of making calls, (e) call general meetings of Co. for obtaining sanction by ordinary or special resolution or for other purposes as he thinks fit.

Wider powers are given to the Liq. in a voluntary winding up than in the case of compulsory winding up. The exercise of his powers, however, is subject to the control of the Court and any creditor or contributory who is aggrieved by his act or proposed act can always apply to the Court under s. 518 of the Act.

A Liq. in voluntary winding up, like a trustee in bankruptcy, is entitled to go behind a judgment against the Co. It is not necessary that fraud or collusion should be shown. It is sufficient if it can be shown that there ought not to have been a judgment, e.g. an *ex parte* decree on a mortgage, which the managing agent had no power to execute and which was void against the Liq. as not having been registered under the Act as required (h).

Duties of Liquidator: The Liq. shall pay the debts of the Co. and shall adjust the rights of the contributories amongst themselves. Where there are more than one Liq., the above powers may be exercised by such one or more of them as may be determined at the time of their appointment and in default of such determination, by not less than 2 of them. No body corporate shall be qualified for appointment as Liq. in a voluntary winding up. Any such appointment shall be void. Such body corporate and every director, managing agent, secretaries and treasurers, and manager of the Co. shall, on violation of the above, be punishable with fine (s. 513). Any person giving or agreeing to give to any member or creditor of the Co. any gratification with a view to secure his own nomination as Liq. or securing or preventing the appointment of another person than himself as Liq. is punishable with fine (s. 514).

Appointment and Removal of Liquidator: If from any cause whatever there is no Liq. acting, the Court may appoint a Liq. The Court, on cause shown, may remove a Liq. and appoint another. The Liq. within 21 days of his appointment, shall publish in the Official Gazette and deliver to the Registrar a notice of his appointment in the prescribed form. Penalty for failure is a fine (s. 516).

Arrangement with Creditors: An arrangement entered into between a Co. about to be or in course of winding up and its creditors shall, subject to right of appeal, be binding on the Co. and on the creditors, if sanctioned by a *special resolution* of the Co. and acceded to by ~~three~~ ^{four} in number and value of the creditors. Any creditor or contributory may, within 3 weeks of completion of the arrangement, appeal to the Court against it and the Court may amend, vary, confirm or set aside the arrangement as it may deem just (s. 517). The powers under the sec. are generally made use of where the Liquidation is to continue over a period, otherwise, powers under s. 391 are more beneficial and proper (i).

Power to apply to Court: S. 518 gives liberty to the Liq., creditor or contributory to apply to the Court (a) to determine any question arising in the winding up of the Co., (b) to exercise in respect of enforcing calls, stay of proceedings or any other matter, all or any of the powers which the Court may exercise in case of compulsory winding up. The Liq. or any contributory or creditor may apply to the appropriate Court for setting aside any attachment, distress or execution put in force against the estate and effects of the Co. after commencement of winding up. Where attachment, distress or execution

(h) Ali Mahomed v. Deccan Match Mfg. Co., 34 Bom. L.R. 411.

(i) Re Cental Radio (1932) 2 Ch. 66.

is levied by the High Court, the application shall be made to the High Court; in other cases, to the Court having jurisdiction to wind up the Co. The Court, if satisfied on such application, that determination of such question or required exercise of its powers would be just and beneficial, may accede wholly or partly to such application on such terms and conditions as it may think fit or make such other order as may seem just. A copy of order staying proceedings in winding up under the sec. shall be forthwith forwarded by the Co., or otherwise as may be prescribed, to the Registrar, who shall enter a minute in respect thereof in his books.

Power to order Public Examination: Under s. 519, the Liq. may make a report to the Court that in his opinion a fraud has been committed by any person in the promotion or formation of the Co. or by any officer relating to the Co. since its formation and the Court may, after considering the report, direct that the person or officer shall attend before the Court on the appointed day and be publicly examined as to the promotion or formation or conduct of business of the Co. or as to his conduct and dealing as officer thereof. The provisions of s. 478, cls. (2) to (11), shall apply to such examination with the substitution of Liq. for Off. Liq. in the said cls.

Compulsory winding up not barred: S. 521 provides that a voluntary winding up shall be no bar to the right of any creditor or contributory to have the Co. wound up by the Court but on a contributory's application the Court must be satisfied that the rights of contributories will be prejudiced by a voluntary winding up. Generally, the Court will not order a compulsory winding up while a voluntary liquidation is pending on a creditors' petition unless (i) the rights of the creditors are injured or (ii) the general body of creditors desire it or, (iii) the Liq. is an unfit person. On a contributory's petition for the same purpose, the Court will not make an order for compulsory winding up unless (i) the voluntary winding up resolution was fraudulently passed or (ii) there are circumstances of suspicion or (iii) a searching investigation is needed (j).

WINDING UP UNDER SUPERVISION

Advantages: The advantages of winding up under supervision are that: (i) it operates automatically as stay of suits and proceedings against the Co. (s. 526); (ii) additional Liq. can be appointed by the Court (s. 524); (iii) checks can be placed by the Court by the relevant order over the powers of the Liq. (s. 523), e.g. of filing accounts with the Registrar, etc.

Winding up under Supervision—When: S. 522 provides that at any time after a Co. has passed a resolution for *voluntary winding up*, the Court may make an order that the same shall continue but subject to such supervision of the Court and with such liberty to creditors, contributories and others to apply to the Court and generally on such terms and conditions as the Court may think just. A petition for winding up under supervision shall, for the purpose of giving jurisdiction to the Court over suits and *legal proceedings*, be deemed to be a petition for winding up by the Court (s. 523). The Court has a discretion under s. 522, both as to whether an order for winding up under supervision should be made and also as to what restrictions should be placed on the powers of Liq. As was held in *Watson and Sons (k)*, the Court has power under the corresponding English sec. to turn a voluntary liquidation into a liquidation by the Court, by placing restrictions on the powers of the Liq. The Court may also, if it thinks fit, relax the restrictions, according to the requirements of the case.

Power to appoint and remove Liquidator: S. 524 provides that where a Court makes a supervision order, the Court may, by the same or subsequent order, appoint additional Liq. or Liq.s. The Court may remove any Liq. so appointed or any Liq. continued under the supervision order and fill any vacancy caused by removal or by death or resignation. A Liq. appointed by Court under s. 524 shall have the same powers and be subject to the same obligations and in all respects stand in the same position as a Liq. appointed under a voluntary winding up (s. 525). A Liq. in winding up under supervision may, subject to any restrictions imposed by Court, exercise all his powers without the sanction or intervention of the Court in the same way as if the Co.

was being wound up voluntarily. Except as provided above, an order for winding up under supervision shall be deemed to be an order for compulsory winding up for all purposes including stay of suits, and other proceedings and shall confer full authority on the Court to make and enforce calls made by Liq.s and for exercising all such powers as would be exercisable by it under a compulsory winding up. In all relevant provisions for the above purpose, "Liquidator" shall be deemed to include Liq. in winding up under supervision (s. 526). Under s. 527, where a supervision order is followed by an order for compulsory winding up, the Court may by the last or any succeeding order appoint the then Liq. or Liq.s (whether provisional or permanent) to be Liq. or Liq.s in winding up by the Court, in addition to and subject to the control of the Off. Liq.

PROVISIONS APPLICABLE TO EVERY MODE OF WINDING UP

Proof and Ranking of Claims: S. 528 provides that in case of every winding up, all debts payable on a contingency and all claims against the Co., present or future, certain or contingent, *ascertained or sounding in damages only*, shall be admissible to proof against the Co., a just estimate being made, as far as possible, of the value of all such debts or claims. In case of insolvent Co.s, this will be subject to the appropriate Insolvency Acts. As laid down by s. 529, in the winding up insolvent Co.s, the same rules shall prevail and be observed as regards (a) debts provable, (b) valuation of annuities, and future and contingent liabilities, and (c) the respective rights of secured and unsecured creditors as are in force for the time being under the Insolvency Law applicable to the parties. All persons who in such case would be entitled to prove for and receive dividends out of the Co.'s assets may come under the winding up and make such claims against the Co. as they are respectively entitled to make by virtue of the aforesaid rule.

A secured creditor in winding up can do either of three things: (i) he can rely on his security and ignore the winding up altogether or (ii) value the security and prove for the balance or (iii) he can surrender the security and prove for the whole debt. An attaching creditor whose attachment has not materialised by sale thereunder, is not a secured creditor by reason only of his attachment (l).

Insolvent Companies: S. 529 makes the same rules applicable in the winding up of an insolvent Co. as are applicable in case of an individual insolvency as regards the following matters: (i) debts provable, (ii) valuation of annuities and future and contingent liabilities, and (iii) the respective rights of secured and unsecured creditors. This had started a controversy in India as to whether all insolvency rule regarding proof of debts, etc. are applicable in a Co. winding up or some of them only. In England, the rules of bankruptcy as regards mutual dealings and set-off, as regards all debts being paid *pari passu*, as to proof by secured creditors and as to lodging proof at any time, so long as the trustee has funds in hand, and as to Crown having a limited priority (m), have been held applicable in winding up of Co.s. However, the rules as regards reputed ownership (n), as regards the landlord's right to distrain for rent accrued due before winding up (o), and as regards duty of secured creditor to surrender or value his security before presenting a winding up petition (p), have not been held applicable. In India, some of the above rules have been followed, while others have been differently enunciated. The Federal Court in *G. G. in Council v. Sheromony Sugar Mills Ltd.* (q), held that the Crown was bound by the provisions of the Companies Act "to a statutory scheme of administration of the assets wherein the prerogative right of the Crown to priority no longer exists" (except as provided by the sec.).

Priority of Debts: After the assets are collected and the claims against the Co. are admitted or proved, the Liq. has next to proceed to pay off and discharge the claims, from the collected assets as far as they would go. In this connection, certain claims against a Co. in liquidation are given statutory priority as regards payment, over other

(l) *Goverdhandas v. Off. Liq.*, 31 Bom. I.R. 1209.

(m) *Food Controller v. Cork* (1923) A.C. 647.

(n) *Gorringe v. Irewell etc. Works* (1886) 34 Ch.D. 128.

(o) *Thomas v. Patent Lionite Co.* (1881) 17 Ch.D. 250.

(p) *Moor v. Anglo Italian Bank* (1879) 10 Ch.D. 681.

(q) (1946) F.L.J. 29.

claims against the Co. S. 530 in this connection provides that in winding up, there shall be paid in priority of all other debts, (a) all revenue, taxes, cesses and rates due to the *Central or State Governments* or to a local authority, which have become due and payable within 12 months next before the "relevant date", (b) all "wages" or salary (including wages due for time or piece work and salary wholly or partly earned as commission) of any employee due for services for a period not exceeding 4 months, during 12 months next before the "relevant date". The amount is not to exceed Rs. 1,000 for each in any case. As regards a labourer in husbandry, employed on a lump-sum annual basis, the proportionate amount payable to him for services as by way of priority, shall be decided by the Court. "Wages" include remuneration in respect of holiday and absence from work through sickness or other good cause; (c) all "accrued holiday remuneration" becoming payable to an employee (or in case of his death, to any other person in his right), on termination of his employment before or by reason of the winding up order or resolution. "Accrued holiday remuneration" includes all sums payable as such in ordinary course in respect of holiday (either under the contract of employment or any enactment or orders made thereunder), had the employment continued till the person became entitled to the holiday; (d) all contributions payable during 12 months next before the "relevant date", by the Co. under Employees' State Ins. Act, 1948, or any other law in force for the time being (except in cases where winding up is voluntary and merely for purposes of reconstruction and amalgamation); (e) all amounts due for compensation under the Workmen's Compensation Act, 1923, for death or disablement of employee [except in cases, (i) where winding up is voluntary and merely for purposes of reconstruction and amalgamation and (ii) where under s. 14 of the above Act, the contractual rights of the Co. with the Insurers are capable of being transferred and becoming vested in the workman). Where such compensation is a weekly payment, the lump sum for which the employer could have redeemed such payment by application under the Act, shall be regarded as the amount payable; (f) all sums due to the employee from a provident fund, gratuity fund or any fund maintained by the Co. for welfare of employees; (g) expenses of investigation under s. 235 and s. 237 so far as payable by the Co.

Where a person has advanced moneys to an employee on account of wages or salary or to him or to another in his right, for accrued holiday remuneration, such person shall have priority for the same, upto the amount by which the sum payable in priority to such employee or other person has diminished by such payment.

The above debts mentioned shall rank equally amongst themselves and shall be paid in full. If the assets are insufficient to pay them in full, they shall abate in equal proportions. They shall also have priority over a floating charge in favour of debenture holders as regards property comprised in the charge. If a landlord or any other person distrains or has within 3 months next before the winding up order, distrained on any goods or effects of the Co., the above debts shall be a first charge on the same or the sale proceeds thereof. In respect of any moneys paid under the above rule, the landlord or other person shall have the same priority as the person to whom the payment is made. The aforesaid debts shall be discharged forthwith, so far as the assets are sufficient to meet them, after retaining necessary sum for costs and expenses of winding up. As regards amount payable under the Employees' State Insurance Act, formal proof shall not be required unless prescribed. The "relevant date" in case of compulsory winding up (which is not preceded by a voluntary winding up), is the date of first appointment of provisional Liq. and if no such appointment has been made, the date of the winding up order; in all other cases, the date of passing of the resolution for voluntary winding up. In case of a Co., the compulsory winding up order in connection with which, and in other cases, the commencement of winding up of which, has taken place before the commencement of the present Act, s. 230 of the Act of 1913 shall apply.

Effect of Winding up on Antecedent Transactions

Fraudulent Preference: S. 531 provides that (i) any transfer of property movable or immovable, delivery of goods, payment, execution, or other act relating to property made, taken or done by or against a Co. *within 6 months before the commencement of winding up* which had it been made, taken or done by or against an individual within 3 months of the presentation of the insolvency petition against him on which he is adjudi-

cated insolvent, would be deemed fraudulent preference in insolvency shall be also regarded as such as regards the Co. and therefore invalid in the event of the Co. being wound up. The period of 3 months shall be substituted for 6 months as regards acts amounting to fraudulent preference which took place before commencement of the Act. (ii) For the above purposes, presentation of the petition for winding up in case of compulsory winding up and winding up under supervision, and passing of resolution for voluntary winding up in case of voluntary winding up, shall be taken to correspond to the act of insolvency in case of an individual.

In deciding whether a case of fraudulent preference is made out, the Court generally looks at the dominant motive which prompted the transaction (r). Where payment is made under a mistaken apprehension that if a particular creditor is not paid, the Co. would be taken into liquidation, fraudulent preference will be negated (s).

S. 532 provides that a transfer or assignment by the Co. of all its property, to trustees for the benefit of all its creditors is void. S. 533 further lays down that if in the case of a Co. being wound up, any fraudulent preference is committed, after the commencement of the Act, in favour of a mortgagee or, or charge holder or any person interested in, the Co.'s property, such favoured person shall be liable for and shall have the same rights as if he were a surety for the same to the extent of the mortgage or charge or the extent of his interest (whichever is less). The sec. makes secured and semi-secured creditors who are fraudulently preferred liable personally to the extent of the debt. The value of the person's interest shall be determined as at the date of the transaction impugned as if it was free from all incumbrances other than those to which the mortgage or charge was then subject. Where a payment is disputed as fraudulent preference of a surety or guarantor the Court shall have jurisdiction to decide all questions relating thereto, by, if necessary, bringing the surety or guarantor on the record as a third party. The sec. applies to cases where fraudulent preference consists of anything other than payment of money. The sec. is intended to provide for those cases where fraudulent preference of surety or guarantor is committed by fraudulently paying off a creditor whose debt is guaranteed by such person so as to relieve such person from liability as surety.

Floating Charge in Winding up: In winding up, a floating charge created on the undertaking or the property of the Co. *within 12 months* of the commencement of the winding up shall, unless the Co. is proved to be solvent immediately after the creation of the charge, be invalid, except to the amount of any cash paid to the Co. at the time of or subsequently to the creation of the charge and in consideration thereof, with interest at 5 per cent per annum or *such other rate as notified by the Central Government in the Official Gazette*, provided that as regards such charges created more than 3 months before the commencement of the present Act, 3 months' period shall be substituted for 12 months' period (s. 534). Floating charges created within 12 months of winding up are declared invalid by the sec., except for the amount of cash actually advanced at the time with interest at 5 per cent, or such other rate as the Central Government may allow. The sec. does not deal with fraudulent issue of debentures. In *Lloyd's Furniture Place* (t), a Co. was formed by A to sell furniture. Instead of subscribing for shares of the Co., A hit upon the plan of advancing loans to the Co. on condition that the Co. should issue a debenture to him for the advances, whenever he called upon the Co. to do so. A was also on the Board of Directors. When the Co. got into difficulties, A applied for and had a debenture issued to him to secure all advances. The creditors were pressing hard but they were kept at bay for the statutory period (3 months as it then was). *Held*, the debenture was valid *prima facie* and was binding on the unsecured creditors. If the floating charge has crystallised into a fixed charge before the winding up commenced, the sec. will not apply (u).

Disclaimer of Onerous Property: Where the property of the Co. consists of land burdened with onerous covenants, or shares or stock, or unprofitable contracts or of any other property not saleable or readily saleable because of its binding the owner to per-

(r) Ex parte Taylor (1886) 18 Q.B.D. 295;
Sharp v. Jackson (1889) A.C. 489; Nabin
Kishore v. Jagneshwar, 37 C.W.N. 909.
(s) Pabna Dhan Bhandar Co. v. Jag-

neshwar, 37 C.W.N. 909.

(t) (1925) Ch. 85.

(u) Re Lewis Marthyr Collieries Ltd.
(1929) 1 Ch. 498.

form any onerous act or to payment of a sum of money, the Liq., notwithstanding that he has taken possession or exercised ownership with regard thereto, may, with leave of Court, by writing signed by him, at any time within 12 months of the commencement of winding up, or such extended time as the Court may allow, disclaim the property. If such property has not come to the knowledge of the Liq., within 1 month after the commencement of the winding up, such period shall be counted from the date, it so comes to his knowledge or such extended period as may be allowed by the Court. The disclaimer, from the date thereof, shall operate to determine all the rights, liabilities and interests of the Co., and its property, in the property disclaimed, but shall not affect the rights or liabilities of any other person. The Court before giving the sanction, may require notices to be given to persons interested and impose terms and conditions, as it deems just. If an application in writing has been made, by any person interested in the property requiring the Liq. to decide whether he will disclaim or not, and he has not, within 28 days of the receipt of the application or such extended time as the Court may allow, given notice to the applicant that he intends to apply to Court for leave to disclaim, the Liq. shall not be entitled to disclaim the same. In case of a contract, if within the said period he does not disclaim it, he shall be deemed to have adopted the same. Where a person is entitled to the benefit of or liable to the burden of a contract as against the Liq., the Court may, on the application of such a person make an order rescinding the contract, on such terms as to payment of damages by either party as the Court thinks just. Such damages can then be proved in winding up. The Court, on the application of any person claiming to be interested in or liable in respect of any disclaimed property, and after hearing such persons as it thinks fit, make an order for vesting or delivery of that property to any person entitled thereto, by way of compensation on such terms as it thinks just. The property shall accordingly vest in such person, without any conveyance, etc. being necessary. If such property is a leasehold, the Court shall not make an order for the vesting thereof in an under-lessee or mortgagee of the same, except on terms making the latter liable for the same liabilities to which the Co. was liable at the commencement of the winding up, or if the Court thinks fit, for the same liabilities, as if the lease had been assigned to such person at that date and as if, in each case, the lease comprised that property alone. If the under-lessee or mortgagee declines to accept the property on the above terms, they shall be excluded from all interest in and security upon the property. If there is no other person who would accept the property on the above terms, the Court shall have power to vest the interest of the Co. in that property in any person liable, personally or in a representative character, and either alone or jointly with the Co. to perform the covenants of the lease, free from all incumbrances thereon. The person injured by the disclaimer, can prove for damages in the winding up (s. 535).

Avoidance of Transfers : In the case of voluntary winding up, any transfer of shares of the Co. not being a transfer made to or with the consent of the Liq. and any alteration in the status of the members of the Co. made after the commencement of winding up shall be void. In the case of compulsory winding up or winding up under supervision, any disposal of the property (including actionable claims) of the Co. and any transfer of shares in the Co. or alteration in the status of its members, made after commencement of winding up shall be void, unless the Court otherwise orders (s. 536). The sec. lays down an important principle of law as regards the disposal of the assets of a Co. pending winding up. Cl. (i) deals with case of voluntary winding up. It provides that in such case, every transfer of shares, unless to or with the sanction of the Liq., shall be void ; also that every alteration of the status of a member, pending liquidation, shall be void. Cl. (ii) goes further and provides that in case of compulsory winding up or winding up under supervision, every disposition of the property of the Co., every transfer of shares or alteration of the status of any member pending liquidation, shall be void, unless sanctioned by the Court.

The fundamental principle in all winding up (as well as bankruptcy), is that all unsecured creditors should be paid *pari passu* and the Court will not tolerate any conduct on the part of the Co. or its directors which has the effect of giving preference to one creditor or set of creditors, over the other creditors of the Co. The Court, however, will under cl. (ii) sanction any *bona fide* transaction carried out and completed in the ordinary course of current business. In an English case, a customer of a trading

Co. had *bona fide* ordered and paid for goods of the Co., the Co. had loaded the goods on railway to his address and sent him the invoices after presentation of petition but before winding up order was passed, *held*, the disposition of property was complete before commencement of winding up and the goods should be ordered to be delivered to the customer (*v*). As regards alteration of status, the principle is the same as that mentioned above. A creditor after a winding up has commenced, will not be allowed to alter his position from that of an unsecured creditor to that of a secured creditor. Specific performance in such a case will be refused.

Enforcement of Duties of Liquidator: A new power is now given to the Court under s. 556. Where a Liq. makes default in filing, delivering or making any return, account or other document or giving any notice, as required by law, after notice to him to make good the same, within 14 days after the service of the notice on him, the Court may order him to make good the default within such time as the Court directs, on the application of a creditor, or contributory of the Co. or of the Registrar. Costs of the order in such case may be thrown on the Liq. Penalties prescribed by other enactments for such default are not to be affected by the above.

Provisions as to avoiding Dissolution: S. 559 provides that where a Co. has been dissolved, whether in pursuance of provisions of Part VII (relating to winding up) or of s. 294 (on reconstruction and amalgamation), or otherwise, the Court can, within 2 years of dissolution, by order declare the dissolution to be void, on the application being made in that behalf by the Liq. or any other person who appears to the Court to be interested, on such terms as the Court thinks fit, and thereupon such proceedings may be taken as might have been taken if the Co. had not been dissolved. Within 21 days of the order or such further time as the Court may allow, the person obtaining the order must file a certified copy thereof with the Registrar, who shall register the same. Penalty for failure is a fine.

Power to strike off Defunct Companies from Register: Under s. 560, (i) where the Registrar has reasonable cause to believe that a Co. is not carrying on business or in operation, he shall send to the Co. by post a letter inquiring whether the Co. is carrying on business or is in operation. (ii) If the Registrar does not within 1 month of sending the letter, receive a reply, he shall, within 14 days after expiry of the month, send by registered post to the Co. a letter referring to the first letter, stating that no answer has been received thereto and further stating that if no answer is received to the second letter within 1 month of the date thereof, a notice will be put up in the Off. Gazette with a view to strike off the Co.'s name from the Register. (iii) If the Registrar within the said month receives answer that the Co. is not carrying on business or is in operation or does not receive any reply thereto, he may publish in the Off. Gazette and send by registered post to the Co. a notice that on expiration of 3 months from date of notice, the Co.'s name will be struck off the Register and the Co. dissolved, unless cause to the contrary is shown. (iv) The Registrar shall send a similar notice as in (iii), if, in case of a Co. being wound up, he has reasonable cause to believe, either that no Liq. is acting or that the Co.'s affairs have been completely wound up, but returns required to be made by the Liq., have not been made for 6 consecutive months. (v) On the expiry of the period of notice, unless cause to the contrary is previously shown, the Registrar may strike the Co.'s name off the Register and publish notice thereof in the Off. Gazette. The Co. shall stand dissolved on publication of notice in the Off. Gazette, provided that (i) the above does not affect the liability of any director, managing agent, secretaries and treasurers or any other officer exercising powers of management and of any member of the Co. and the same may be enforced as if the Co. had not been struck off the Register, (ii) the above does not affect the power of the Court to wind up a Co. whose name has been struck off the Register. (vi) The Co. or a member or creditor thereof, may, if aggrieved by the Co.'s name being struck off as above, within 20 years of publication of notice in the Off. Gazette, apply to the Court and if the Court is satisfied that the Co. was at the relevant time carrying on business or was in operation or otherwise that it is just that the Co. should be restored to the Register, it may by order direct the Co.'s name to be restored and make such provisions as may seem just for placing the Co. and all other persons in the same position as nearly as may be, as if the Co.'s

name had not been struck off. (vii) On a certified copy of the order under (vi) being delivered to the Registrar for registration, the Co. shall be deemed to have continued in existence, as if its name had not been struck off. (viii) Letters and notices under the sec. may be addressed to the Co. at its registered office, and if it has none such, to the care of some director, managing agent, secretaries and treasurers, manager or other officers and if the address of any such is not known, to each of the persons who subscribed to the Memo., at the address therein mentioned. (ix) Notice to the Liq. under the sec., may be addressed at his last known place of business.

Power to compromise : Under s. 546, a Liq. may (a) with the sanction of the Court when the Co. is being wound up by or under the supervision of the Court and (b) with the sanction of a special resolution in case of voluntary winding up (i) pay any classes of creditors in full; (ii) make a compromise or arrangement with creditors or alleged creditors or claimants or alleged claimants, whether present or future, certain or contingent, ascertained or sounding in damages only or whereby the Co. may be made liable; (iii) compromise any call, or liability to call, debt or liability capable of resulting in debt and any claim present or future, certain or contingent, ascertained or sounding in damages only, subsisting or alleged to be subsisting between the Co. and a contributory or alleged contributory or other debtor or a person apprehending any liability to the Co. and all questions in any way relating to or affecting the assets, liabilities or the winding up, on such terms as agreed, and take security for and give complete discharge for the same; (iv) in case of voluntary liquidation, the Liq.'s powers shall be subject to the control of Court; (v) any creditor or contributory may apply to Court with respect to any exercise or proposed exercise of such power.

Misfeasance : S. 543 provides that where in the course of winding up a Co., it appears that any person who has taken part in the formation or promotion of the Co. or any past or present director, managing agent, secretaries and treasurers, manager, or Liq., or officer of the Co. has misapplied or retained or become liable or accountable for any money or property of the Co. or has been guilty of any misfeasance or breach of trust, in relation to the Co., the Court may, on the application of the Off. Liq., Liq. or any creditor or contributory made within 5 years of the winding up order or the first appointment of the Liq. in the winding up or of the misapplication, retainer, misfeasance or breach of trust, as the case may be, whichever is longer, examine into the conduct of such person and compel him to repay or restore the property or money or any part thereof respectively, with interest at such rate as the Court thinks just, or to contribute such sum to the assets of the Co. by way of compensation, in respect of the misapplication, retainer, misfeasance or breach of trust, as the Court thinks just. The sec. shall apply notwithstanding that the offence is one for which the offender may be criminally responsible. Where a declaration under s. 543 is made by the Court in respect of a firm or body corporate, the Court shall also have power to make a similar declaration against any person who, at the relevant time, was a partner or director respectively of the firm or body corporate (s. 544).

The sec. provides a summary procedure for bringing negligence or fraudulent directors and other persons connected with the administration of a Co. to book. It does not create new rights and liabilities (w). As Evershed M.R. pointed out in *Re Johnson and Co.* (x), "there is no such distinct wrongful act known to law as 'misfeasance'". "Misfeasance" means a breach of duty, resulting in loss to the Co. James L.J. said in *Coventry and Dixon's Case* (supra): "I am of opinion that the word 'misfeasance' in the sec. means misfeasance in the nature of a breach of trust, that is to say, it refers to something which the officer of such Co. has done wrongly by misapplying or retaining in his own hands any moneys of the Co. or by which the Co.'s property has been wasted or the Co.'s credit improperly pledged. It must be some act, resulting in actual loss to the Co." A misfeasance summons against directors can be taken out by the liquidator when a private Co. goes into liquidation, even though the directors concerned are the only directors and also the only shareholders of the Co. (x1).

(w) *Coventry & Dixon's Case* (1880) 14 Ch.D. 660.

(x) (1955) 2 All E.R. 775.

(x1) *Banaji v. Manilal*, A.I.R. (1956) Bom. 681.

Protection of Directors and others: S. 633 provides that if in any proceedings for negligence, default, breach of duty, misfeasance or breach of trust, against an "officer" of the Co., it appears to the Court that that person is or may be liable in respect of the negligence, default, breach of duty, misfeasance or breach of trust, but that he has acted honestly and reasonably and that having regard to all the circumstances of the case, including those connected with his appointment, he ought fairly to be excused, the Court may relieve him, either wholly or partly, from his liability, on such terms as the Court may think fit. Where any such "officer" has reasons to apprehend that any claim will or might be made against him in respect of any negligence, default, breach of duty, misfeasance or breach of trust, he may apply to the Court for relief and the Court shall have the same power to relieve him, as if proceedings against him for the same had been started in that Court.

The sec. is intended to protect the Officers of a Co. from liability for honest mistakes or errors of judgment causing loss to the Co. In such cases, though their conduct may technically amount to a breach of trust or misfeasance, the Court has jurisdiction to release them from liability. The words "having regard to the circumstances, including those connected with their appointment" are intended to protect persons who become directors, etc. because of their expert knowledge of the special business of the Co. Such persons cannot be expected to look into the detailed management of the Co.'s affairs and the Court will, therefore, relieve them from liability under the present sec.

In order to obtain protection of the sec. the person concerned has to satisfy the Court, not only that he acted honestly and reasonably, but also that his conduct had been such that he ought fairly to be excused. Thus where a director acts honestly but not reasonably, the Court has no power to grant relief under the sec. (1). Where directors, who had validly delegated their powers to the managing director, allowed the managing director to gamble in differences on the stock exchange, it was held that the directors were guilty of grave breach of duty and therefore could not be excused under the sec. (2).

Prosecution of Delinquent Directors, etc.: S. 545 provides that if in course of a winding up by or under the supervision of the Court, it appears to the Court that any present or past officer, or member, of the Co. has been guilty of an offence in relation to the Co., the Court may, either of its own motion or on the application of any person interested, direct the Liq. to prosecute the offender or refer the matter to the Registrar. If in course of a voluntary winding up a similar thing appears to the Liq., he shall forthwith report the matter to the Registrar and give him all information and access to relevant documents, as are under his control. Where a report is made as above to the Registrar, he may refer the matter to Central Government for further inquiry. The latter can, in such a case, apply to the Court for an order conferring all powers of investigation to an officer designated by them, as are available in winding up. The Registrar, if he thinks that no proceedings ought to be taken by law, shall inform the Liq. accordingly and thereupon the latter, with sanction of the Court, may take the same. If in course of a voluntary winding up, it appears that any of the above persons is guilty as aforesaid but no report has been made to the Registrar in respect thereof, the Court may, on the application of any person interested or on its own motion, direct the Liq. to make the report and cl. (2) of the sec. shall thereupon apply. Where the Registrar considers that in any matter aforesaid, a prosecution ought to be instituted, he shall report the matter to the Central Government and if advised by them, he may institute proceedings. No such report, however, shall be made without giving the person concerned an opportunity of making a statement in writing to the Registrar and of being heard thereon. The Liq. and all officers and agents of the Co. (including banker, legal adviser and auditor of the Co.) shall be bound to give him all assistance in their power. The Court, on the application of the Registrar, may direct any person to comply with the sec. and in case of the Liq., to direct him to pay the costs personally.

Unclaimed Dividends and Undistributed Assets: In all cases of winding up the Liq. shall forthwith pay into the Public Account of India in the Reserve Bank, all moneys

(y) Doss v. Connel, A.I.R. (1937) Mad. 124; Peninsular Locomotive v. Reed (1937) Pat. 293.

(z) Thinappa v. Rajagopalan (1944) 2 M.L.J. 85.

which represent unclaimed dividends or undistributed assets, payable or refundable to a creditor or contributory respectively and which have remained in his hands or under his control for 6 months from the date they become so payable or refundable; (ii) on dissolution also, the Liq. shall pay all such moneys into the said account which remain in his hands at the date of dissolution. (iii) While making any such payment, the Liq. shall furnish to the prescribed officer a statement with respect to all sums paid in showing their nature, the names and the last known addresses of the persons concerned, the amount to which each is entitled, the nature of his claim and other prescribed particulars, (iv) The Liq. shall be entitled to a receipt from the Reserve Bank for such payment which shall be a sufficient discharge. (v) Where the Co. is being wound up by the Court, the Liq. shall make such payment by transfer from the account mentioned under s. 552. (vi) In case of voluntary winding up and winding up under supervision, the Liq. shall indicate in the annual statements to be filed by him under s. 551, the amount in his hand or under his control in the above behalf within 6 months preceding the date of the statement and shall pay the same into the Companies Liquidation Account within 14 days thereafter. (vii) Persons claiming any moneys paid into the above account (a) may apply to the Court for such payment. Notice must thereupon be given to the prescribed officer to show cause within one month of service, why payment should not be made. The Court if satisfied about the claim, may make a payment order thereafter. (b) Such person can also apply to the Central Government for such payment. If satisfied by the certificate of the Off. Liq. or the Liq. or otherwise and if no application has been made to Court for such payment by any other person, the Central Government may order payment to such person after taking sufficient security from him. (viii) If moneys in the above account remain unclaimed for 15 years, they will be transferred to the general revenue account of the Central Government. Any claim for payment is not however to be affected thereby, order for refund being treated as refund of revenue. A Liq. not complying with the above provisions is liable to pay interest on the amount retained at 12 per cent and also such penalty as may be determined by the Registrar. He will also be liable to pay the expenses caused by his default, in cases of winding up by the Court or under supervision; his remuneration also may be disallowed and he may also be removed from office (s. 555).

Bona Vacantia: It has been held in England that the Crown's right to property of a dissolved foreign corporation is a defeasible right and liable to be defeated therefore, if a winding up order is made in another country, e.g. England, with regard to assets of such dissolved foreign corporation situate in England, after notice to the Crown.

CHAPTER XVI

INSOLVENCY *

Insolvency Acts: The law of insolvency in India generally is contained in two enactments, viz. the *Presidency Towns Insolvency Act* which applies to the Presidency Towns (Bombay, Calcutta and Madras) and the *Provincial Insolvency Act* which applies to the mofussil, i.e. the whole of the rest of India except Part B States and the scheduled districts. Both the Acts are based on the English Bankruptcy Act, many of the provisions of the latter being bodily incorporated in the former two. It has been held therefore that decisions on the English Bankruptcy Acts may be looked at where necessary in construing the provisions of the Indian enactments (w).

Scheme of the Acts: Generally the proceedings are started by a petition filed either by the debtor or a creditor of the debtor for the adjudication of the debtor as insolvent. On such petition, the Court adjudges the debtor insolvent, if certain conditions are satisfied. The immediate result of such adjudication is that all the insolvent's property vests in the Official Assignee (under the Presidency Towns Insolvency Act) or the Court

* For a detailed study of the subject, see "Principles of Insolvency Law" by the same author.

(w) Abdul Kader v. Off. Assignee, 40 Mad. 810.

or receiver as the case may be (under the Provincial Insolvency Act). The other result is that thereafter, the insolvent gets the protection of the Court against his creditors executing their decrees against him or filing suits against him. The insolvent has thereafter to file his schedule, which is a statement in a tabulated form of his financial position generally, i.e. of his assets, debts, outstandings, etc. The Court, thereafter, through its officer, the Official Assignee or the receiver investigates into the affairs of the insolvent, examines the insolvent and others who have had connection with or knowledge of the same, considers the claims of the creditors against insolvent and finally after realising his property and estate, distributes the same amongst the creditors in proportion to their claims. The insolvent in the meanwhile, is entitled to ask for and may obtain his discharge, if he has satisfied all the requirements of the Acts and has not been guilty of any illegal or improper conduct. By obtaining his discharge the insolvent becomes a free man again and all his debts and liabilities, so far as allowed by the Court, are wiped out.

Courts exercising insolvency jurisdiction: In the Presidency towns, the Courts exercising insolvency jurisdiction are the High Courts of Calcutta, Madras and Bombay and in the mofussil, the District Court and such other subordinate Court or Courts as may have been invested with insolvency jurisdiction by Government notification. A Court of Small Causes is, for the above purpose, deemed subordinate to the District Court.

Jurisdiction and powers of Insolvency Courts

A Court exercising insolvency jurisdiction has, subject to the provisions of the Acts, full power to decide all questions whatsoever, whether of law or of fact including all questions of priorities (i) which may arise during the course of any insolvency proceedings or (ii) which the Court deems expedient or necessary to decide for the purpose of doing complete justice or making a complete distribution of the property in each case (x). The decisions of the Insolvency Courts are final and binding between the debtor and his estate on the one hand and the claimants and persons claiming through them on the other. Further, where the Court does not deem it expedient to decide any question of title to any property of the debtor but has reason to believe that the debtor has a saleable interest in the property, it is competent to the Court, without further inquiry, to sell off the interest for whatever it is worth (y).

Generally the rule followed by the Insolvency Courts is that they would assume jurisdiction in matters *arising out of insolvency*, even though strangers are affected thereby, e.g. to set aside a fraudulent preference; but they would decline to exercise jurisdiction against a stranger, when the matter arises *outside insolvency*, i.e. when it is unconnected with and arises independently of it (z). Notice, however, that the jurisdiction is purely discretionary. Thus it has been held that where complicated questions of title are likely to arise the Insolvency Court will ordinarily refer the Official Assignee to a separate suit (a). It has been held however that Provincial Courts have exclusive jurisdiction in cases with regard to voluntary transfers and fraudulent preferences arising under the Provincial Act (b).

Acts of insolvency

The acts of insolvency on which an insolvency petition may be founded are as follows (c):

(i) If in India or elsewhere the debtor makes a transfer of all or substantially all his property to a third person for the benefit of his creditors generally.

(ii) If in India or elsewhere he makes a transfer of his property or any part thereof with intent to defeat or delay his creditors.

(x) Sec. 7 Pres. T. Ins. Act; sec. 4 Prov. Ins. Act.

(y) Sec. 4 Prov. Ins. Act; sec. 68 Pres. T. Ins. Act.

(z) *Jnanendra Bala Devi v. Off. Ass.*, 30 C.W.N. 346.

(a) *Off. Ass. v. Vedavalli Amal*, 40 Mad. 810.

(b) *Kaniz v. Narayan*, 49 All. 71.

(c) Sec. 9 Pres. T. Ins. Act; sec. 6 Prov. Ins. Act.

(iii) If in India or elsewhere he makes any transfer of his property or any part thereof which would under the Insolvency Acts or any other law in force, be void as fraudulent preference if he were adjudged insolvent.

(iv) If with intent to defeat or delay his creditors, (a) he departs from or remains out of India, (b) he departs from his dwelling house or usual place of business or otherwise absents himself, (c) he secludes himself so as to deprive his creditors of the means of communicating with him.

(v) If any of his property is sold or (under the Pres. T. Ins. Act) attached for a period of not less than 21 days, in execution of the decree of any Court for the payment of money. (Under the Prov. Ins. Act, attachment of the debtor's property, for however long a time, is no ground for founding an insolvency petition.)

(vi) If he petitions to be adjudged an insolvent.

(vii) If he has given notice to any of his creditors that he has suspended or is about to suspend payment of his debts.

(viii) If he is imprisoned in the execution of the decree of any Court for the payment of money.

(ix) If, after a creditor has served an "insolvency notice" on him in respect of any decree or order for payment of money he does not, within the period specified in the notice, comply with the requirements of the same. Non-compliance with the "notice" however will not amount to an "act of insolvency", if the debtor has a counter-claim or set-off against the creditor, for an amount equal to or greater than the amount ordered to be paid by him, which he could not set up in the suit or proceeding in which the order was made against him (d).

Insolvency notice

This last refers to a "notice" to be given by a creditor to the debtor, calling upon him to pay up the decretal amount (which may be any figure), or give sufficient security for the payment of the same, within the time mentioned in the notice, and further intimating to him that failure to comply with the terms of notice would be regarded as an "act of insolvency". The "notice" is in a prescribed form and is given through Court. The debtor either complies with the "notice" or himself takes out a notice of motion to set aside the insolvency notice. No person, however, other than a holder of a decree or order for payment of money against the debtor, can take out any such "notice". Further, execution of such decree or order must not have been stayed by an order of the Court. The decree or order may be for any amount. It has been recently held in Bombay (e) that if the debtor shows *prima facie* that he has a counter-claim which he could not set up in the suit in which the decree was obtained the notice will be set aside and the Court will not go into the question, whether the counter-claim is time-barred or not.

Notice that "the act of insolvency" may be committed by and through an agent also. As regards *Gumasta* or *Munim* in native firms, it has been held (f) that it is a question of fact in each case whether the *Gumasta* occupies such a position that the principal stands or falls by his acts. The same rule applies with regard to partners also (g). It has been recently held by the Privy Council that where an Insolvency Court holds a transfer by a debtor as fraudulent and as an act of insolvency, the transferee is bound by the decision also and it will therefore be *res judicata* against him unless he appeals therefrom as a person aggrieved under sec. 8 of the Prov. Act (h).

Insolvency petition: When an act of insolvency has been committed as above, an insolvency petition may be presented, subject to certain rules, either by a creditor or by the debtor, and the Court, if satisfied that such an act has been committed and that the petition satisfies the other statutory requirements, may make an order adjudicating

(d) Sec. 9A Pres. T. Ins. Act; sec. 6A Prov. Ins. Act.

(e) *Faramroz v. Hormasjee*, 48 Bom. L.R. 737.

(f) *Kasturchand v. Dhanapat Singh*, 23 Cal. 26.

(g) *Gopal v. Mohanlal*, 49 Mad. 189.

(h) *Mahomad Siddique v. Off. Ass., Calcutta*, 47 Bom. L.R. 522.

the debtor insolvent. The petition should clearly set forth the grounds of insolvency bringing the case within any one or more of the above cls. If the facts alleged do not constitute an act of insolvency, no subsequent amendment will be allowed and the petition will be dismissed. Notice that no petition can be presented against an incorporated company which is registered under the Companies Act (sec. 107, Pres. Act; sec. 8, Prov. Act). For such companies proceedings in the nature of liquidation and winding up have to be adopted under the Indian Companies Act.

General conditions for insolvency jurisdiction

The Court has no power to make an order of adjudication unless: (i) the debtor at the time of the presentation of the petition is imprisoned in execution of a money decree in any prison to which debtors are ordinarily committed by the Court in the exercise of its ordinary original civil jurisdiction or (ii) the debtor within a year before the date of the presentation of the insolvency petition has ordinarily resided or has a dwelling house or has carried on business himself or through an agent within the limits of the ordinary original jurisdiction of the Court or (iii) the debtor personally works for gain within those limits or (iv) in case of petition by or against a firm unless the firm has carried on business within a year before the date of the presentation of the petition, within those limits (i). The Prov. Act contains no limitations as regards the length of residence for carrying on business, etc. Under it the place where the debtor is in custody also gives jurisdiction (j).

Conditions for a creditor's petition: The conditions for a creditor's petition are: (i) that the debt owing by the debtor or if two or more creditors join in the petition the aggregate amount of debts owing to such creditors is rupees five hundred. If the creditor is a secured creditor, he should state in his petition whether he is willing to relinquish the security for the benefit of the creditors in the event of adjudication or give an estimate of the value of the security. In the latter case he will rank as a creditor for the balance of the debt remaining after deducting the value of the security and not for the whole debt. (ii) That the debt is a liquidated sum payable either immediately or at a certain future time. (iii) That the act of insolvency on which the petition is grounded occurred within three months before the presentation of the insolvency petition. Notice that though a decree of Court is *prima facie* evidence of a debt, the Insolvency Court is not necessarily bound by it. It can go behind it and inquire whether the debt was really or validly due and whether the decree was obtained by fraud, collusion, etc. (k).

Conditions for a debtor's petition: A debtor cannot present an insolvency petition unless (i) his debts amount to Rs. 500 or (ii) he has been arrested and imprisoned in execution of a decree of a Court for the payment of money or (iii) unless an order for attachment in execution of such decree is made and is subsisting against his property (l). Under the Prov. Act (m) a debtor shall not be entitled to present an insolvency petition unless (a) he is unable to pay his debts and (b) (i) his debts amount to Rs. 500 or (ii) he is arrested or imprisoned in execution of a money decree or (iii) unless an order for attachment in execution of a money decree is made and is subsisting against his property. The sec. further provides that (c) where an order of adjudication made against a debtor is subsequently annulled owing to his failure to apply for or prosecute his application for discharge, the debtor shall not be allowed to present an insolvency petition without the leave of the Court by which the adjudication was annulled. Such Court shall not grant leave unless it is satisfied (i) that the debtor was prevented by reasonable cause from presenting or prosecuting the application for discharge or (ii) that the petition is founded on facts substantially different from those contained in the petition on which the first order of adjudication was made.

Procedure: Hearing of petition: Under the *Presidency Act* (n), at the hearing of a creditor's petition: (i) the Court shall require proof of (a) the debt of the petitioning creditor; (b) the act of insolvency or if more than one such acts are alleged, of any one of such acts. (ii) The Court may adjourn the petition and order service thereof on the

(i) Sec. 11 Pres. T. Ins. Act.

(j) Sec. 11 Prov. Ins. Act.

(k) *Rc Fraser* (1892), 2 Q.B. 633.

(l) Sec. 14 Pres. T. Ins. Act.

(m) Sec. 10 Prov. Ins. Act.

(n) Sec. 13.

debtor. (iii) The Court shall dismiss the petition (a) if it is not satisfied as to the facts referred to in cl. (i) above or (b) if the debtor appears and satisfies the Court that (i) he is able to pay his debts or (ii) that he has not committed an act of insolvency or (iii) that for other sufficient cause no order ought to be made, e.g. where the petition appears to be an abuse of the process of the Court (o). (iv) The Court may make an order of adjudication (i) if it is satisfied as to the proof of the above facts or (ii) if, where the hearing is adjourned, the debtor does not appear at the adjourned hearing and service of the petition on him is proved, unless the Court is of opinion that the petition should have been presented to some other Court having jurisdiction. (v) Where the debtor appears and denies the debt or the sufficiency of the amount thereof the Court shall stay all proceedings on the petition instead of dismissing the same, for such time as may be required for the trial of the question relating to the disputed debt after taking such security (if any) from the debtor as the Court thinks reasonable. (vi) Where proceedings are stayed as above the Court may, if it thinks just, make an adjudication order on the petition of any other creditor and thereupon it shall dismiss the petition on which proceedings were stayed on such terms as to costs as it may think just. At the hearing of a debtor's petition the debtor must prove that he is entitled to present a petition. The Court may thereupon make an order of adjudication, unless in its opinion the petition ought to have been presented to some other Court having jurisdiction. The Court however may dismiss the petition if it finds that the debtor has not furnished to the Official Assignee a list of his creditors and has not deposited his books of account with him. The debtor is bound to do these things as soon as his petition is admitted (p).

Under the Prov. Act (q), (i) when an insolvency petition is admitted, the Court shall make an order fixing a date for hearing the petition. (ii) Notice of the order admitting the petition shall be given to creditors in such manner as may be prescribed. Where the debtor is not the petitioner, notice of the order admitting the petition shall be served on him in the manner provided for service of summons. (iii) On the day fixed for the hearing of the petition or any subsequent day to which the hearing may be adjourned, the Court shall require proof (a) that the creditor or the debtor as the case may be is entitled to present the petition provided that where the debtor is the petitioner he shall for proving his inability to pay his debts be required to furnish only *prima facie* proof of the said fact; (b) that the debtor, if he does not appear on a petition presented by a creditor, has been served with notice of the order admitting the petition; (c) that the debtor has committed the act of insolvency alleged against him. (ii) The Court shall also examine the debtor if he is present as to his conduct, dealings and property in the presence of such creditors as appear at the hearing and the creditors too shall have the right to question the debtor thereon. (v) The Court shall dismiss the creditor's petition if (a) the Court is not satisfied as to his right to present the petition, (b) is not satisfied as to the service on the debtor of the order admitting the petition, (c) is not satisfied as to the alleged act of insolvency, (d) or is satisfied by the debtor that he is able to pay his debts or (e) that for any other cause no order ought to be made. (vi) Where a petition by a creditor is dismissed and the Court is satisfied that the petition was frivolous or vexatious, the Court may award against the creditor such amount not exceeding Rs. 1,000 as the Court thinks reasonable compensation to the debtor for the injury and expense caused to him by the proceedings. (vii) The Court shall dismiss the debtor's petition if it is not satisfied as to his right to present the same. (viii) If the Court does not dismiss the petition it shall make an order of adjudication thereon and shall specify the period within which the debtor shall apply for his discharge. The Court may, if sufficient cause is shown, extend the period within which the debtor shall apply for his discharge and in that case shall publish notice of the order in such manner as it thinks fit. Notice that under both the Acts (r), neither the debtor's nor a creditor's petition can after presentation be withdrawn without the leave of the Court. If a creditor neglects to appear on his petition, no subsequent petition shall be presented by the creditor against the same debtor individually or jointly with others with respect to the same act of insolvency without the leave of the Court (Bom. Ins. Rule 65). If a debtor does not prosecute his petition or does not obtain his discharge within such time as may

(o) *Re Ballav Chand*, 27 Cal. W.N. 739.

(p) Sec. 15 Pres. T. Ins. Act.

(q) Sccs. 18-25.

(r) Sec. 15 Pres. T. Ins. Act; sec. 14 Prov. Ins. Act.

be prescribed, the Court may annul the adjudication or make such other order as it may think fit (s).

Interim proceedings before order of adjudication: (i) *Interim Receiver:* Under Pres. Act the Court may if it is shown necessary for the protection of the estate at any time after presentation of a petition and before adjudication, appoint the Official Assignee to be interim receiver of the property of the insolvent or part thereof and direct him to take immediate possession thereof.

Under Prov. Act the Court when admitting the petition may and *where the debtor is the petitioner shall, appoint an interim receiver of the property of the insolvent or part thereof and direct him to take immediate possession thereof.*

(ii) *Security against and arrest of debtor:* Under the Prov. Act the Court at the time of admitting the petition or any subsequent time before adjudication, (a) order that the debtor should give reasonable security for his appearance until final orders are made on his petition and that in default he may be committed to civil prison; (b) order any property in the possession or control of the debtor and liable to attachment under the Civil Procedure Code (including his books of account) to be attached; (c) order that a warrant of arrest be issued against the debtor with or without bail for his arrest and directing him to be detained in civil prison till the disposal of the petition or that he should be released on giving reasonable security. The above provisions are absent in the Pres. Act as under that Act there is practically no interval between the presentation of the petition and the order of adjudication to be made thereon.

(iii) *Interim Protection:* This is an order by an Insolvency Court granting protection to the debtor from arrest and imprisonment at the instance of a creditor in execution of a money decree obtained by him till a formal protection order is passed (t). Under the Prov. Act there is no provision for granting such interim protection to the debtor on the presentation of an insolvency petition, the only power granted to the Court being that under sec. 23 of the Act, viz. to release a debtor if he is already under arrest or imprisonment on such terms as to security as the Court thinks just. Under the Pres. Act, insolvents are granted interim protection as a matter of course on an order of adjudication being made against them. Such protection generally however cannot be granted till the insolvent has filed his schedule.

(iv) *Duties of the debtor on the presentation of an insolvency petition:* Every debtor who has filed a petition must forthwith lodge with the Official Assignee or Receiver all papers, vouchers, account books, etc. relating to his estate together with a statement of his moveable and immoveable properties (u).

Order of adjudication: The Court may, if the petition for adjudication satisfies the requirements of law as stated above, make an order of adjudication (v). Notice of every order of adjudication with name, address and description of the insolvent, the date of adjudication, the Court by which the order is made and the date of the presentation of the petition shall be published, in case of the Presidency Towns in the Gazette of India, local Official Gazette and in such other manner as may be prescribed, and in case of the provincial towns, in the local Official Gazette and such other manner as may be prescribed.

Effect of order of adjudication

On making of the order of adjudication—(i) All the property of the insolvent shall in the case of the Presidency Towns vest in the Official Assignee and in the case of the Provinces vest in the Court or the Receiver and shall be divisible amongst his creditors. (ii) Thereafter except as directed by the respective Acts, no creditor to whom the insolvent is indebted in respect of a debt provable in insolvency shall, during the pendency of the insolvency proceedings, have any remedy against the property of the

(s) Sec. 41 Pres. T. Ins. Act; sec. 43 Prov. Ins. Act.

(t) Sec. 25 Pres. T. Ins. Act.

(u) Sec. 15 Pres. T. Ins. Act; sec. 22 Prov. Ins. Act.

(v) Sec. 10 Pres. T. Ins. Act; sec. 7 Prov. Ins. Act.

insolvent in respect of the debt or shall commence any suit or other legal proceedings, except with the leave of the Court and on such terms as the Court may impose. (iii) Nothing in the respective secs. however affects the power of a secured creditor to realise or otherwise deal with his security in the same manner as he would have, had the sections not been passed (*w*). The effect of the secs. is to vest all the property of the insolvent moveable as well as immoveable in the Official Assignee or the Court or Receiver as the case may be as soon as an order of adjudication is made. The order operates as a statutory transfer to the Official Assignee of all the property of the insolvent in India, whether moveable or immoveable (*x*). As regards foreign property, the better opinion is that moveables will vest in the officer concerned; but immoveable property will not so vest, unless foreign law permits it (*y*).

The consequences of the vesting of all property of the insolvent in the Official Assignee or the Receiver are: (i) after adjudication the insolvent cannot deal with or enter into transactions with third parties with respect to the property. That power, after adjudication, is vested in the Official Assignee alone and he alone can give title to a purchaser. (ii) The insolvent cannot afterwards file a suit in his own name to recover part of his property from a third person. (iii) The insolvent after adjudication cannot prosecute a suit filed by him before adjudication. It is only the Official Assignee who can do so. (iv) The Court may also, at any time after making the order of adjudication, stay any suit or other proceeding pending against the insolvent before any Judge or Judges of the Court or in any other Court subject to its superintendence. A Court in which proceedings are pending against a debtor, may also on proof of an adjudication order against the debtor stay all proceedings or allow them to continue on such terms as it thinks just. The first of the above powers is not given to Provincial Courts (*z*). (v) The Court may also appoint a special manager for such period as it may think fit to assist the Official Assignee if in its opinion it is necessary having regard to the debtor's business or to the interest of the creditors generally. No such power is given to Provincial Insolvency Courts.

Annulment of adjudication

The Court may annul the adjudication if—(i) In the opinion of the Court the debtor ought not to have been adjudged insolvent. (ii) Where it is proved to the satisfaction of the Court that the debts of the insolvent are paid in full: For this purpose any debt disputed by the debtor shall be considered to be paid in full if the debtor enters into a bond with approved sureties to pay the amount of the debt and costs of recovering the same if established by law. Secondly, a debt due to a creditor who cannot be found shall be deemed to be fully paid if paid into Court. The application can be made by any person interested. (iii) The Court may also on its own motion, or on application of Official Assignee or any creditor, annul adjudication if the petition is presented by a person not entitled to do so. (iv) Where it is proved to the satisfaction of the Court that insolvency proceedings are pending in any other Indian Court, whether within or without the States against the same debtor and the property of the debtor can be more conveniently administered there, the Court may annul the adjudication or stay all proceedings thereon. (v) An adjudication shall be annulled on the Court approving a composition or scheme of arrangement (see seq.). (vi) If the insolvent does not appear on the day fixed for hearing his application for discharge or does not apply to the Court for discharge within the time prescribed, the Court may annul the adjudication or make such other order as it thinks just. (vii) Also, where insolvency proceedings are pending in a Court subject to the superintendence of the High Court (*a*).

Proceedings on annulment: (i) Where an order of adjudication is annulled, all sales and dispositions of property and payments duly made and all acts theretofore done by the Official Assignee or other person under his authority or by the Court or Receiver under the Prov. Act, shall be valid, but the property of the debtor shall vest in such person

(*w*) Sec. 17 Pres. T. Ins. Act; sec. 28 Prov. Ins. Act.

(*x*) Off. Ass. of Bombay v. Registrar, Small Causes, 37 I.A. 86.

(*y*) Yokohama Specie Bank v. Curlenders & Co., 43 Cal. L.J. 436.

(*z*) Secs. 21, 22, 30 & 41 Pres. T. Ins. Act; secs. 35 & 43 Prov. Ins. Act.

(*a*) Sec. 18A Pres. T. Ins. Act.

as the Court may appoint and in the case of failure to appoint, shall re-vest in the debtor to the extent of his right and interest therein subject to such terms as the Court may impose. (ii) Where the debtor is released from custody on being adjudicated insolvent he shall be liable on annulment of adjudication to be re-arrested and re-committed to jail. (iii) Notice of the order of annulment shall be published in the Gazette of India and the local Official Gazette and in such other manner as may be prescribed. Under the Prov. Act notice is to be published in the local Official Gazette and in such other manner as may be prescribed. Ordinarily, the Court, when annulling adjudication, imposes terms on the debtor, e.g. by transferring his property to a third person for the benefit of his creditors. This is usually done when adjudication is annulled on the Court approving a composition; because, this is in effect a continuance in another form of the original insolvency. As the debtor reverts to his own original position on annulment of adjudication, he can continue a suit filed by the Official Assignee or Receiver during his insolvency; the suit does not abate on annulment (b). Where an order of adjudication is annulled, the property of the insolvent which was vested in the Official Assignee or Receiver automatically reverts to the debtor. No order of the Court is necessary. All proceedings taken against such property during the intervening period will also be validated (b1). Notice that where adjudication is annulled, a creditor of the insolvent gets the benefit of the period during which the petition was pending, for saving limitation, in case he has to file a suit thereafter to establish his claim (c).

Proceedings consequent on adjudication: Schedule: (i) Where an order of adjudication is made against a debtor he shall prepare and submit to the Court a schedule verified by affidavit in such form and containing such particulars as may be prescribed. The "schedule" is generally a statement on oath or solemn affirmation by the insolvent with regard to his property, debts, outstandings, etc. (ii) In case of a debtor's petition it shall be submitted within 30 days of the date of the order of adjudication and in the case of a creditor's petition within 30 days of the service of the said order on the debtor. (iii) If the insolvent fails to comply with the above requirement, the Court may order the debtor to be detained in a civil prison. (iv) The Official Assignee also may, in such case, himself cause a schedule to be prepared of the insolvent's estate at the expense of the estate (d). Under the Prov. Act there is no provision for a schedule similar to the above. Under that Act the Court is required to prepare a schedule of creditors of the insolvent.

Protection Order: This is an order for which, an insolvent, who has submitted his schedule, may apply to the Court for protection from arrest or detention in execution of decrees, etc. (e). Protection may be granted by the Court with regard to all debts mentioned in the schedule or some of them and may commence at and take effect for such time as the Court may direct. The Court may also at any time renew or revoke the same. No such order however shall operate to prejudice the right of any creditor in the event of the order being subsequently varied or if the adjudication is subsequently annulled. Any creditor shall be entitled to appear at the hearing of the application for protection and oppose the granting of the same, but the insolvent shall be *prima facie* entitled to such order on production of a certificate signed by the Official Assignee that he has so far confirmed with the provisions of the Act. A protection order may be granted before the insolvent has filed his schedule, if the Court thinks it necessary to do so in the interest of the creditors. The Prov. Act lays down practically the same provision except that under that Act protection order can be made only after an adjudication order has been passed. The object of a protection order is to prevent a debtor, after he has officially declared his inability to pay his debts, from being harassed by his creditors. The protection order has the effect of relegating all the creditors to an equal footing and of securing that the distribution of the debtor's estate shall proceed evenly and in accordance with law.

Public Examination of the Insolvent: After the Court makes an order of adjudication, it is required to hold a public sitting on a day to be appointed by the Court

(b) Haji Sajan v. N. C. Macleod, 32 Bom. 321.

(b1) Parvathi v. Easo, A.I.R. (1955) Tr.-Co. 241.

(c) Sec. 101A Pres. T. Ins. Act; sec. 78 Prov. Ins. Act.

(d) Sec. 24 Pres. T. Ins. Act.

(e) Sec. 25 Pres. T. Ins. Act.

after notice to creditors for the examination of the insolvent. The insolvent must attend such meeting, where he will be examined as to his conduct, dealings and property. The examination must be held as soon after as convenient after expiration of time for filing the schedule. Any creditor who has tendered a proof or a legal practitioner on his behalf may question the insolvent concerning his affairs and the causes of his failure. The Official Assignee shall take part in the examination of the insolvent and for that purpose, subject to the directions of the Court, may appear by a legal representative. The Court may put such questions to the insolvent as it thinks expedient. The insolvent shall be examined upon oath and it shall be his duty to answer all questions put by or allowed to be put by the Court to him. Notes of his examination shall be taken down in writing and shall be read over and signed by him. They may thereafter be used against him in evidence and shall be open to inspection of any creditor at all reasonable times. Where the Court is of opinion that the insolvent's affairs have been sufficiently investigated, it shall by order declare the examination to be concluded, but such order shall not prevent the Court from directing further examination of the insolvent whenever it thinks fit to do so. When the insolvent is a lunatic or suffers from any mental or physical disability making him unfit, in the opinion of the Court, to attend his public examination or is a woman who does not appear in public, the Court may make an order dispensing with the examination or directing it to take place at such time and place as the Court deems expedient (g).

The above examination of the insolvent is called "*public examination*" in contradistinction with the examination of persons under sec. 36, which is called "*private examination*". The object of the examination under this section is to inquire into the "conduct, dealings and property" of the insolvent, in other words, a general inquiry into his affairs. The inquiry is not limited to offences connected with insolvency but extends to all matters which the Court may take into consideration on the application for discharge. Notice that under the Prov. Act the examination is held before the order of adjudication is made (h). Applications for the public examination of the insolvent must be made before the insolvent applies for his discharge. Except in special circumstances, such applications will not be granted after the insolvent's application for discharge is put on board for hearing (i).

Composition and schemes of arrangement

A "composition" is a settlement by an adjudged insolvent with his creditors, by payment to them of something less than the amount actually due; a "scheme" is an arrangement by a debtor with his creditors, whereby, in due course of time, the amounts due to them will be liquidated (generally by payment of an amount less than that actually due). A debtor may compound with his creditors without having recourse to the Insolvency Court. The question considered here is of compositions entered into by debtors *after* adjudication. These are valid and binding only if approved by the Court. Under the Pres. Act (j) at any time after adjudication, the insolvent may submit to the Official Assignee a proposal in the prescribed form for a composition of his debts with his creditors or a scheme of arrangement of his affairs with the same view. The Official Assignee shall thereupon send to each creditor who is mentioned in the schedule or who has proved his debt before him a copy of the said proposal with his report thereupon. A meeting of the creditors will then be called and if on a consideration of such proposal (a) the majority in number and (b) three-fourths in value of all creditors whose debts are proved, resolve to accept the proposal, it shall be deemed to be accepted by the creditors. The insolvent at the meeting may amend the terms of his proposal if the same is beneficial to the general body of creditors. After the proposal is accepted by the creditors, the insolvent or the Official Assignee may apply to the Court to approve the same. Notice of the day appointed for hearing the application must be given to all creditors who have proved. Unless the estate is being summarily administered or special leave has been obtained, *such application cannot be heard until the public examination of the insolvent is finished*. Any creditor who has proved, may appear before the Court and be heard in opposition to the application, though he may have voted for the proposal

(g) Sec. 27 Pres. T. Ins. Act.

(h) Sec. 23 Prov. Ins. Act.

(i) Re Furdunji D. Daruwalla, 26 Bom.

L.R. 627.

(j) Secs. 28-29.

at the meeting. The Court shall before approving also hear the report of the Official Assignee as to the terms of the proposal and as to the conduct of the insolvent. It may also hear the Official Assignee. It shall also hear any objections by or on behalf of any creditor.

The Court shall refuse to approve the proposal if in the opinion of the Court, (a) the terms of the proposal are not reasonable or (b) not calculated to benefit the general body of creditors or (c) in case facts are proved which require the Court to refuse the insolvent's discharge. (d) Where facts are proved which would require the Court either to refuse, suspend or attach conditions to the debtor's discharge, the Court shall refuse to approve the proposal unless it provides reasonable security for payment of not less than 4 annas in the rupee on all unsecured debts provable against the debtor's estate (under the Prov. Act 6 annas). (e) No composition or scheme can be approved which does not provide for payment in priority of all debts so directed to be paid by the Act in the distribution of the insolvent's estate. (f) In any other case also, the Court may either approve or refuse to approve the proposal. (g) The Court can also refuse to approve a composition or arrangement in certain cases of fraudulent, anti-nuptial and post-nuptial marriage settlements. (h) The Court will not approve a composition or scheme accepted by creditors unless it provides for the due payment of the costs, charges, expenses and remuneration of the Official Assignee.

Procedure on approval of composition or scheme: Under the Pres. Act (k), if the Court approves of the proposal, the terms thereof shall be embodied in an Order of the Court and thereupon an order shall be made annulling the adjudication. The order shall be notified in the Government Gazette. The estate of the insolvent shall thereupon vest in such person as the Court may direct and in default of such direction shall revert to the debtor. Any person interested in the composition or scheme may apply to the Court for the enforcement of the terms thereof and any disobedience to the order of the Court made on such application will be deemed a contempt of Court. Under the Prov. Act (l) also, the terms of the composition or scheme are, on approval, to be embodied in an order of the Court. The Court however has thereafter to frame a schedule of creditors and the composition will be binding on all creditors entered in the schedule so far as relates to claims therein entered.

Effect of approval of composition: The effect of an approval of an arrangement or scheme by the Court is (i) that the adjudication is annulled, (ii) the property of the insolvent re-vests in him and (iii) all the creditors of the insolvent are bound thereby so far as regards any debts due to them from the insolvent and provable in insolvency. (iv) On annulment of adjudication the provisions relating to consequences of annulment will apply (m). Notice that under the Prov. Act the composition binds *only those creditors who are entered in the Schedule and that too only to the extent of their debts entered therein* (n). If default is made in payment of any instalment in pursuance of a composition or scheme approved by the Court or if it appears to the Court that the composition or scheme cannot proceed without injustice or undue delay or that the approval of the Court has been obtained by fraud, the Court may, on the application of any person interested, if it thinks fit, readjudicate the debtor an insolvent and annul the composition or scheme and thereupon all the property of the debtor shall re-vest in the Official Assignee, but without prejudice to any transfer or payment duly made by the insolvent during the interval (o).

Duties of the insolvent after adjudication: (i) The insolvent shall, unless disabled by sickness or other sufficient cause, attend such meeting of his creditors as the Official Assignee requires him to attend and give such information as the meeting may require. (ii) The insolvent shall further, (a) give such inventory of his property, such lists of his creditors and of debts due to and from him respectively, (b) submit to such examination as to his creditors or property, (c) meet at such times and places the Official Assignee or Special Manager, (d) execute such powers of attorney, transfers and instruments and (e) generally do all such acts and things in relation to his property and the distribution

(k) Sec. 30.
(l) Sec. 39.
(m) Sec. 30.

(n) Sec. 39.
(o) Sec. 31.

of the proceeds thereof amongst his creditors, as may be required by the Official Assignee or Special Manager or as may be prescribed or directed by the Court by any special order or orders. (iii) The insolvent shall further aid to the utmost of his powers in the realisation of his property and the distribution of the proceeds thereof amongst his creditors. (iv) If the insolvent fails to perform the duties imposed upon him as above he shall be liable for contempt of Court. Failure to perform some of the duties is an offence also under the Acts. (v) If it appears to the Court that the insolvent has absconded or is about to abscond with a view to avoid examination or otherwise defeating, insolvency proceedings against him, or that he is about to remove his property with a view to prevent or delay possession thereof being taken by the Official Assignee or if he removes any property in his possession above Rs. 50 in value without the leave of the Official Assignee, the Court may order his arrest. (vi) The Court may direct that for a certain period, not exceeding three months, all postal communications addressed to the insolvent shall be redirected to the Official Assignee (p).

Examination under sec. 36: (i) The Court on the application of the Official Assignee or any creditor who has proved his debt may after an order of adjudication is made, summon before it the insolvent or any person known or suspected to have in his possession any property belonging to the insolvent or supposed to be indebted to the insolvent or any person whom the Court may deem capable of giving information respecting the insolvent, his dealings or property. The Court may also require such person to produce any document in his custody or power relating to the insolvent, his dealings or property. (iii) If the person summoned, after being tendered a reasonable sum, refuses to come before the Court at the appointed time or to produce any document without any lawful excuse allowed by the Court, the Court may cause him by warrant to be arrested and brought up before it. (iv) The Court may examine a person so brought up before it, concerning the insolvent, his dealings and property. Such person may be represented by a legal practitioner. (v) If on such examination *such person admits* that the person is indebted to the insolvent, the Court may on the application of the Official Assignee order him to pay the debt or part thereof to the Official Assignee either in full discharge of the debt or not, as the Court thinks fit, and with or without costs of examination. If on such examination *such person admits* that the person is in possession of any property of the insolvent, the Court may on the application of the Official Assignee order him to deliver possession thereof to him on such terms as the Court may think fit. A similar power is given to Court by the Prov. Act also (q).

The examination under sec. 36 is called "private examination". Its object is to gather information and to obtain discovery of the insolvent's property and dealings for the benefit of the Official Assignee, with a view to enable him to decide what further action he should take with regard to them. Orders under sec. 36 are purely discretionary. The guiding principle is that it should be for the benefit of the general body of creditors as a whole and not for the benefit of the particular creditor who is applying for the same. Thus a person who has filed a suit against the insolvent will not be allowed to invoke the section in order to get information to support his case (r). It has been held that an examination of the insolvent or any third person under sec. 36 can be held even after the discharge of the insolvent (s).

Discharge

After the insolvent has filed his schedule and his affairs are sufficiently investigated, he proceeds to obtain his discharge. Under the *Pres. T. Ins. Act* (t), (i) at any time after adjudication the insolvent can apply to the Court for an order of discharge and the Court shall fix a day for hearing the application in open Court but except where public examination under sec. 27 is dispensed with, the application shall not be heard until such examination is concluded.

(ii) At the hearing of the application, the Court, after considering the report of the Official Assignee as to the insolvent's conduct and affairs may: (a) grant or refuse an

(p) Secs. 33-34 *Pres. T. Ins. Act*; sec. 22 *Prov. Ins. Act*.
(q) Sec. 51A.

(r) *Re Easton*, 8 Mor. 168.
(s) *Shadhan Chandra v. Shivnarayan*, 60 Cal. 936.
(t) Secs. 38, 44.

absolute order of discharge, (b) suspend the operation of the order for a specified time or (c) suspend the discharge until a dividend of not less than four annas has been paid to the creditors, or (d) require the insolvent as a condition precedent to his discharge to consent to a decree being passed in favour of the Official Assignee for any unsatisfied balance or part thereof of his debts provable in insolvency, the same to be paid out of his future earnings or income or after-acquired property in such manner as the Court may direct.

(iii) The Court shall *refuse the discharge where* (a) the insolvent has committed any offence under the Act (e.g. fraudulent concealment of estate by destruction of deeds, keeping false books of account, giving fraudulent preference, etc.) or (b) under the Indian Penal Code (fraudulent deeds and disposition of property).

(iv) The Court may (a) either refuse the discharge or (b) suspend or (c) attach conditions to the discharge in any manner specified above: (a) if the insolvent's assets are not equal to four annas in the rupee of his unsecured liabilities and he fails to satisfy the Court that the fact that they are not of such value has arisen from circumstances for which he cannot be justly held responsible; (b) if the insolvent has failed to keep such books of account as are usual and proper in the business carried on by him and which sufficiently disclose his business transactions and financial position within three years immediately preceding the insolvency; (c) if the insolvent has continued to trade after knowing that he was in insolvent circumstances; (d) if he has contracted any debt provable in insolvency, which at the time of contracting he had no reasonable or probable ground for believing he would be able to repay. The burden of proving this would be on the insolvent; (e) if the insolvent has failed to account satisfactorily for any loss of assets or deficiency of assets; (f) if he has brought on the insolvency by rash or hazardous speculations, by unjustifiable extravagance in living or by gambling or by culpable neglect of his business affairs; (g) if the insolvent has put any of his creditors to unnecessary expense by defending a suit properly brought against him by frivolous and vexatious defences; (h) if the insolvent has within three months preceding the presentation of the insolvency petition incurred unjustifiable expense by filing a frivolous and vexatious suit; (i) if within three months preceding the presentation of the insolvency petition and while unable to pay his debts he has given undue preference to any of his creditors; (j) if the insolvent has concealed or removed his books of account or his property or any part thereof or has been guilty of any other fraud or fraudulent breach of trust. (k) The Court can also refuse or suspend the discharge or grant it subject to conditions in the following cases: (a) in case of a settlement made before or in consideration of marriage, where the settler was at the time not in a position to pay all his debts without the aid of the property comprised therein, and (b) in case of a covenant for future settlement on the settler's wife or children in consideration of marriage, where the settler had at the time of marriage no interest or estate in the property or money comprised therein (other than that in the right of his wife), if the settler is adjudged insolvent or compounds or arranges with his creditors, and it appears to the Court that the settlement, covenant or contract was made to defeat or delay creditors or was unjustifiable having regard to the settler's affairs at the time.

(v) The power of suspending and imposing conditions to the discharge may be exercised concurrently.

(vi) Where a decree is passed against the insolvent in favour of the Official Assignee as laid down above, to be paid out of the earnings, income or after-acquired property of the insolvent, such decree cannot be executed without the leave of the Court and such leave will be granted only on proof that the insolvent has since his discharge acquired property or income available for payment of his debts.

(vii) On the application for discharge the report of the Official Assignee shall be *prima facie* evidence and the Court may presume the correctness of any statement therein made.

Notice that death of insolvent does not bring about automatic discharge of the insolvent and the insolvency proceedings do not terminate thereon. The creditors are

entitled to prove their claims after the death of the insolvent until an unconditional order of discharge is passed (t1).

Discharge under Prov. Act: The *Prov. Act* lays down nearly similar provisions with regard to the subject of discharge, except that under this Act, there is no rule as to suspension of discharge till a certain proportion of the debts is paid. Similarly, there is no provision under the Act for passing a decree against the insolvent for the balance of unpaid debts. There is also no absolute bar to discharge in cases where offences against Insolvency Law or the Penal Code are proved (u). The object of discharge is to relieve the insolvent from all liabilities for his debts except in so far as the order of discharge otherwise provides. The insolvent after his discharge becomes a free man again. The Court therefore is very careful to scrutinise all the facts relating to the insolvency before granting a discharge. The Court has a very wide discretion in the matter of granting or refusing a discharge. The discretion however is to be exercised on judicial principles. In considering the question of discharge the Court will look not only to the interests of the insolvent and the creditors but also to the interests of public and commercial morality (v). It will consider whether the insolvent has been guilty of any of the acts or neglects mentioned in sec. 39. Over and above that, however, it will also consider the conduct of the insolvent generally and grant or refuse him discharge accordingly. Notice however that the conduct referred to above is not any conduct but conduct relevant to the insolvency.

When the Court refuses the discharge the insolvent may, with leave of the Court, renew the application after such time and under such circumstances as may be prescribed. When an order is made subject to conditions, the insolvent can at any time after two years from the date of the order satisfy the Court that there is no reasonable probability of his being able to comply with the terms of the order. The Court if so satisfied may modify the terms of the order on such terms and conditions as it may think fit. The provisions of the *Prov. Act* are similar (x).

Effect of discharge

An order of discharge generally releases the insolvent from all debts provable in insolvency. It does not release the insolvent however from (a) any debt due to the Crown, (b) any debt or liability incurred by means of fraud or fraudulent breach of trust to which he was a party, (c) any debt or liability in respect of which the insolvent has obtained forbearance by means of fraud to which he was a party, (d) any liability for maintenance under the Criminal Procedure Code. (e) The order of discharge does not release any person who at the date of the presentation of the petition was a partner, or a co-trustee, co-debtor or a co-contractor with the insolvent or any person who was a surety of or in the nature of a surety for him (y).

The effect of these clauses is that the discharge releases the debtor from a debt, even though the debt and the name of the creditor to whom it is owing have been omitted from the schedule and the creditor has in fact no notice of the insolvency. As regards the *excepted debts*, note that a debt due by the insolvent to a Government soap factory has been held to be a "Crown debt". Similarly, a promoter of a limited company who has obtained secret profits from the vendors is not discharged from liability for what amounts to his breach of trust. Discharge also does not release a debtor from debts incurred by him after adjudication, though before his discharge, because these are not debts provable in insolvency. A discharge does not operate as a termination of the insolvency. Even after discharge the Insolvency Court has jurisdiction to give directions as to the distribution of the assets, and if they have been wrongly distributed, to order them to be re-distributed according to legal principles. Similarly, a creditor who has not proved before discharge can always come in and prove his debt so long as there are assets in hand; provided he does not thereby disturb a prior distribution of assets

(t1) *Puttathama v. Chicha Venkappa*,
A.I.R. (1957) Mys. 3.

(u) Secs. 41, 42.

(v) *Rc Badcock*, 3 *Morr.* 138.

(w) Sec. 40.

(x) Secs. 41-43.

(y) Sec. 45 *Pres. T. Ins. Act*; sec. 44 *Prov. Ins. Act*.

(z). Notice that a discharge by an Indian Court cannot bind a foreign Court, though it may be recognised by all Indian Courts as valid. An Order of discharge passed by a foreign Court has been held to be binding on an Indian Court (z1).

Debts provable in insolvency: All debts and liabilities, present or future, certain or contingent, to which the debtor is subject when adjudicated insolvent or to which he may become subject before his discharge by reason of an obligation incurred before adjudication, are deemed to be debts provable in insolvency. The exceptions are: (i) demands in the nature of unliquidated damages arising otherwise than by reason of a contract or breach of trust, cannot be proved; (ii) a person having notice of the presentation of an insolvency petition by or against a debtor shall not prove for any debt or liability incurred by the debtor subsequent to such notice. (iii) Where in case of a debt or liability, which, by reason of being subject to contingency or otherwise, does not bear a certain value, the Official Assignee certifies that the value thereof is incapable of being fairly estimated, the debt or liability will be deemed to be a debt not provable in insolvency (a).

Under the wide words of the sec., it has been held that a landlord can prove for prospective damage caused to him by the trustee disclaiming an onerous lease. A lessor can prove for loss of rent or any other liability in respect of a subsisting lease. A claim for devastavit against an executor, a claim for a legacy liable to be paid in the future and a claim for an annuity liable to be divested subsequently can also be proved. A contingent liability on a contract to indemnify can be proved (b). Claims for damages in respect of a fraud cannot be proved unless of course they fall within any of the exceptions. So also claims for damages in respect of torts unless they have been ascertained before adjudication. Notice that a debt contracted after presentation of petition but before order of adjudication is not provable in insolvency. Illegal debts and debts against the policy of insolvency law (e.g. agreement to pay for not opposing discharge) are not provable in bankruptcy. Notice that debts which are barred at the commencement of insolvency cannot be proved but if not so barred, lapse of time does not debar a creditor's right of proof (c).

Set-off in insolvency: Under the Pres. Act. (i) where there have been mutual dealings between an insolvent and a creditor proving or claiming to prove a debt under the Act, an account shall be taken of what is due from one party to the other in respect of such mutual dealings and the sum due from one party shall be set off against that due by the other and the balance of the account and no more shall be claimed or paid by either side respectively. (ii) A creditor shall not be allowed to claim set-off against the property of the debtor, in any case where he had notice of the presentation of an insolvency petition by or against the debtor when he gave credit to him (d). The right of set-off can be claimed only where there are mutual dealings between the insolvent and the creditor. The claims in respect of which set-off can be had, include all debts and demands provable in insolvency. Thus a claim for damages, provided it arises out of contract can be set off against a claim for a liquidated sum. The debts to be set off must however be between the same parties. Thus a joint debt cannot be set off against a separate debt and vice versa. Both parties must also fill the same character; thus a debt due to a testator cannot be set off against a claim against his executor. Notice that "mutual dealings" includes both mutual credits and mutual debits. The words refer to mutual dealings at the time of the insolvency and cannot refer to the purchase of a claim against the insolvent after insolvency by one of the debtors of the insolvent's estate.

Proof of debts: Under the Pres. Act (e), every proof shall be lodged as soon as may be after the order of adjudication is made. The proof of any debt is lodged by delivering to the Official Assignee or by sending by registered post an affidavit verifying the debt. The Official Assignee shall examine every proof and within 30 days of the

(z) *Re Ramchandra Ganuji*, 29 Bom. L.R. 1167.

(z1) *Subramanya v. Shankara* (1956) 1 Mad. L.J. 527.

(a) Sec. 46 Pres. T. Ins. Act; sec. 34 Prov. Ins. Act.

(b) *Hardy v. Fothergill*, 13 A.C. 351.

(c) *Ex Parte Ross*, 64 E.R. 866.

(d) Sec. 47 Pres. T. Ins. Act; sec. 44 Prov. Ins. Act.

(e) Schedule II.

receipt thereof, in writing, admit or reject it, either in whole or in part or call for further evidence. If he rejects a proof he shall state to the creditor in writing his reason for so doing.

A *secured creditor* can (i) realise his security and prove for the balance of his claim, or (ii) he can surrender his security for the benefit of creditors generally and prove for the whole debt. (iii) If he does neither, he shall, before ranking for a dividend, state in his proof the particulars of the security, the date when it was given and the value at which he assesses it. He shall then be entitled to a dividend after deducting from his claim the value of the security as so assessed. The Prov. Act contains analogous provisions, except that under it, it is the Court which determines who the creditors of the insolvent are and frames a schedule. The proofs are therefore lodged before and are examined and accepted or rejected by the Court (f).

With regard to *interest*, the provisions are: (i) on any debt or sum certain on which interest is not reserved or agreed upon and which is overdue at the time of adjudication and which is provable under the Act, a creditor may prove for interest at a rate not exceeding 6 p.c. per annum, (a) if the debt is payable by virtue of a written instrument at a certain time, from the time when such debt or sum was payable to the date of the adjudication; (b) if the debt or sum is payable otherwise, from the time a demand in writing has been made giving the debtor notice that interest will be claimed from the date of demand until the time of payment, to the date of such adjudication. (ii) Where interest has been agreed upon and the debt proved includes such interest or any pecuniary consideration in lieu thereof, the interest (or consideration) for the purpose of dividend shall be calculated at a rate not exceeding 6 p.c. per annum only. This however does not prejudice the right of the creditor to receive out of the debtor's estate any higher rate of interest that may be agreed upon, after all the debts proved have been paid in full.

Priority of debts: Subject to the exceptions mentioned below, all debts proved in insolvency shall be paid rateably according to their respective amounts and without any preference (g). The exceptions are: (a) all debts due to the Crown or any local authority, e.g. Municipal Taxes, Land Revenue, etc.; (b) salary and wages due to any clerk, servant or labourer in respect of services rendered during four months before the date of the presentation of the insolvency petition provided the amount in case of each clerk does not exceed Rs. 300 and in respect of each servant or labourer Rs. 100 in all (Rs. 20 for all, under the Prov. Act); (c) rent due to a landlord, not exceeding one month's (not so under the Prov. Act). After an adjudication order is made, a landlord cannot distrain for rent due before the order was made unless the adjudication is annulled but he can prove for the rent in insolvency.

The aforesaid debts rank equally between themselves and shall be paid in full before any other debts are paid, but if the insolvent's property is not sufficient to meet them they shall abate in equal proportion between themselves.

Subject to the retention of such sums as may be necessary to meet the expenses of the administration, the above debts shall be discharged forthwith so far as the property of the insolvent is sufficient to meet them.

In case of partnerships, the partnership property shall be applicable in the first instance in payment of the partnership debts and the separate property of each partner shall be applicable in the first instance in the payment of the separate debts. If a surplus remains out of the partnership property, it shall be dealt with as the separate property of each partner in proportion to his respective share in the partnership. If a surplus out of the separate property remains after satisfying the separate creditors, it shall be dealt with as part of the partnership property of the partners. This is because partners are jointly and severally liable for all debts of the partnership.

Where there is a surplus after paying all the above debts, it shall be applied in payment of interest at the rate of 6 per cent on all debts proved in insolvency from the date of adjudication till payment.

(f) Secs. 45-50.

(g) Secs. 49-50 Pres. T. Ins. Act; sec. 61 Prov. Ins. Act.

The doctrine of "relation back"

Under sec. 51 of the Pres. Act, (i) the insolvency of a debtor whether it takes place on a debtor's petition or on that of a creditor or creditors, shall be deemed to have "relation back" and to commence at (a) the time of the commission of the act of insolvency on which the order of adjudication is made, or (b) if the insolvent is proved to have committed more than one act of insolvency, the time of the first act of insolvency proved to have been committed by the insolvent within three months next preceding the date of the presentation of the insolvency petition. (ii) No insolvency petition or order of adjudication however shall be rendered invalid by reason of any act of insolvency committed earlier to the debt of the petitioning creditor.

The above sec. is enacted for the purpose of and is therefore restricted to questions relating to the collecting of the assets of insolvent debtors from third parties. The sec. lays down that the insolvency of a person and therefore the title of the Official Assignee in cases of insolvency shall be deemed to date, not from the time when the order of adjudication was made but "relates back", i.e. starts as from the date on which the act of insolvency, on which the petition is grounded, was committed. The result is to ante-date the commencement of insolvency of a person to the date of the commission of the act of insolvency on which the petition is founded, and when more than one such act is committed, to the first act of insolvency committed by the insolvent within three months preceding the presentation of the insolvency petition. The practical effect of this provision is that all dispositions of property, etc. by the insolvent after the act of insolvency on which the petition is founded, would be open to challenge by the Official Assignee even though they are before adjudication, and if objectionable, will be liable to be set aside by him. Notice that transfers made before three months of the presentation of the insolvency petition would give good title to *bona fide* purchasers for value without notice. Under the Prov. Ins. Act, the order of adjudication relates back and takes effect from the date of the presentation of the petition on which it is made (h).

Property available for payment of debts

Under the Pres. Act, the property of the insolvent divisible amongst his creditors (called the "property of the insolvent") shall, with the exceptions noted below, include (i) all property as may belong to or be vested in the insolvent at the commencement of the insolvency or may be acquired by or devolve on him before his discharge; (ii) the capacity to exercise and to take proceedings for exercising all such powers in and over or in respect of property as might have been exercised by the insolvent for his own benefit at the commencement of the insolvency or before his discharge; (iii) all goods being at the commencement of the insolvency in the possession, order or disposition of the insolvent in his trade or business, with the consent and permission of the true owner, under such circumstances that he is the "reputed owner" thereof. (iv) Things in action (other than debts due and growing due to the insolvent in the course of his trade or business) shall not be deemed to be goods within the meaning of cl. (iii). (v) The true owner whose goods have become divisible amongst the creditors of the insolvent under cl. (iii) can always come in and prove for the value of such goods in insolvency.

The exceptions mentioned above are: (i) property held by the insolvent in trust for another person; (ii) the tools (if any) of his trade, necessary wearing apparel, bedding, cooking utensils and furniture of himself, his wife and children, not exceeding in all Rs. 300 in value. The provisions of the Prov. Ins. Act are with slight variations to the same effect (i).

On adjudication all property of the insolvent vests in the Official Assignee under sec. 17 of the Pres. Act. This section defines what property actually does so vest. Under cl. (i), it has been held that the benefit of a contract as well as the burden passes to the Official Assignee and he must elect within a reasonable time whether he will take under the contract or repudiate it (j). Notice however that damages recovered by an insolvent in respect of a personal injury suffered by him do not pass to the Official Assignee and

(h) Sec. 28.

(i) Sec. 52 Pres. T. Ins. Act; sec. 28 Prov.

Ins. Act.

(j) Grey v. Walker, 40 Cal. 523.

cannot be divided amongst creditors. It is only rights of action relating directly to the insolvent's property which so pass. The right, title and interest of an employee in moneys standing to his credit in Provident Fund Account will vest in the Official Assignee on his insolvency, although such moneys are not presently payable to him or have been nominated by him in favour of a creditor (j1). On adjudication, the property of the insolvent in a foreign State does not vest in the Receiver (j2).

After-acquired property: Cl. (i) also deals with what is called the "after-acquired property" of the insolvent, i.e. "property acquired by the insolvent after his adjudication and before his discharge". The result of vesting is that the insolvent cannot thereafter deal with the property or dispose it off. This is invariably so with regard to property acquired by the insolvent before adjudication. Notice however that as regards after-acquired property the rule is that the insolvent can validly deal with such property or dispose it off in favour of third persons any time before the Official Assignee has intervened. This is called *the Rule in Cohen v. Mitchell* (k). It may be shortly stated as follows: "Until the trustee intervenes all transactions by a bankrupt, after his bankruptcy, with any person dealing with him *bona fide* and for value, with respect to his after-acquired property, whether with or without knowledge of bankruptcy, are valid against the trustee". In India the rule has been applied by all the High Courts (except Madras) (l) to moveable as well as immoveable property. For the rule to apply however two things are essential: (i) the transaction must be in good faith and for value, good faith here required being in the person dealing with the bankrupt and not the bankrupt himself, and (ii) the transaction must be effected before the trustee intervenes. Thus where an undischarged insolvent had filed a suit with regard to his after-acquired property and obtained judgment thereon and the decree was subsequently satisfied before the Official Assignee intervened, it was held that the judgment debtor had obtained a good discharge and that he could not be sued to pay over the amount again to the Official Assignee (m). It has been recently doubted whether the rule in *Cohen v. Mitchell* applies to cases under the Prov. Ins. Act, having regard to the fact that under sec. 28(4) of that Act the after-acquired property of the insolvent vests in the Receiver "forthwith" (n). This has been held by the Privy Council to mean "from the date of acquisition or devolution" (o). Bombay however has applied the doctrine to cases falling within the Prov. Ins. Act (p).

Under cl. (ii) of sec. 52, if the insolvent is possessed of certain rights of ownership, etc. over or with respect to certain property which he can exercise for his own benefit, they would under this cl. vest in the Official Assignee, e.g. the right of a Hindu father to alienate his son's share in joint family property for the payment of his own debts (q). The son's share, however, does not automatically vest in the Official Assignee, on the insolvency of the father (r).

Reputed ownership: Cl. (iii) of sec. 52 above deals with what is called "reputed ownership" of goods, etc. Goods of which a person is the reputed owner within the meaning of this cl. would vest in the Official Assignee on the insolvency of the person. By reason of this, goods which are not really the property of the insolvent may be brought within the ambit of the estate of the insolvent if certain conditions are satisfied. These conditions are: (i) the property must be goods, (ii) in the possession, order or disposition of the insolvent, (iii) at the commencement of the insolvency, (iv) in his trade or business, (v) with the consent of the true owner thereof, (vi) under such circumstances that he is the reputed owner thereof. Thus if a purchaser of or holder of a charge over goods allows them to remain with the debtor in embarrassed circumstances, he will lose the benefit of his purchase or charge if the debtor subsequently becomes insolvent and the goods are found in the possession of the debtor. The doctrine does not

(j1) *Muktilal v. Trustees of Tin Plate Co.*, A.I.R. (1956) S.C. 336.

(j2) *Jayantilal v. Kantilal*, 56 Bom. L.R. 1028.

(k) 25 Q.B.D. 262.

(l) *Alimahomed v. Vadilal*, 43 Bom. 890.

(m) *Rozario v. Mohamad*, 26 Bom. L.R. 695.

(n) *Satyanarayanamurthi v. Papayya* (1941). 2 M.L.J. 834; see also *Re Pasco* (1944), 1 Ch. 219.

(o) *Kala v. Jagannath*, 54 I.A. 90.

(p) *Nagindas v. Ghelabhai*, 44 Bom. 673.

(q) *Satnarayan v. Beharilal*, 27 Bom. L.R. 135.

(r) *Shripad v. Bassappa*, 27 Bom. L.R. 935.

apply to immoveable property, nor to "fixtures". An equity of redemption is also not "goods". "Trade debts" are goods within the meaning of the sec. and they would pass to the Official Assignee if the requisite conditions are fulfilled. Notice however that other things in action, e.g. shares, stocks, policies of insurance, share in a partnership, are not included. Property held by trustees on trust also, will not pass under this cl. as long as they are holding it consistently with the trust (s). The reason is that, in such a case, the trustee insolvent is not a "reputed owner" but a true owner. The same is also true of executors, administrators, factors for sale and bailees, provided their possession as such is sufficiently notorious. Goods held under a hire purchase agreement, however, it is held, pass to the Official Assignee.

Insolvency and antecedent transactions

(i) **Execution of decrees:** Under the Pres. Act (t), where execution of a decree has been issued against the property of the debtor, no person shall be entitled to the benefit of the same as against the Official Assignee except (a) in respect of the assets realised in course of execution by sale or otherwise (b) before the date of the order of adjudication and (c) before such person had notice of the presentation of an insolvency petition by or against the debtor. The rule, however, does not affect the rights of secured creditors in respect of property against which a decree is executed. A purchaser in good faith of the debtor's property under an execution sale in all cases acquires good title against the Official Assignee. Where execution of a decree has been issued against any property of a debtor, and before sale, notice is received by the Court executing the decree that an order of adjudication has been made against the debtor, the Court shall, on application, direct that the property, if in the possession of the Court, should be delivered to the Official Assignee. The above provisions have been held not to apply to the administration of the estate of a deceased insolvent (u).

(ii) **Voluntary transfers:** Under the Pres. Act any transfer of property (a) not being a transfer made before and in consideration of marriage or (b) made in favour of a purchaser or incumbrancer in good faith for valuable consideration, shall, if the transferor is adjudged insolvent within two years after the date of the transfer, be void against the Official Assignee. (Under the Prov. Act the period starts from the date of the presentation of the petition.) (v). The sec. makes all voluntary transfers by the debtor within two years of his adjudication, void against the Official Assignee.

Certain transfers are however protected. They are (1) anti-nuptial settlements in consideration of marriage and (2) transfers in favour of persons who take *bona fide* and for value. The good faith required by the sec. is in regard to the transferee and not the transferor. Notice that it has been held that where a transfer of property made by an insolvent is challenged by the Receiver or Official Assignee, the onus is on the latter to prove that the transfer is void against him, and not on the transferee that the transfer is good and valid (w). It has also been held in a series of cases that the Insolvency Court has exclusive jurisdiction to decide questions arising under these secs. (x).

(iii) **Fraudulent preference:** Under the Pres. Act (y) every transfer of property, every payment made, every obligation received and every judicial proceeding taken or suffered by any person (a) who is unable to pay his debts as they become due out of his own moneys (b) in favour of a creditor (c) with a view of giving that creditor preference over other creditors shall (d) if such person is adjudged insolvent on a petition presented within 3 months after the date thereof, be deemed fraudulent and void against the Official Assignee. The sec. does not affect the rights of persons taking in good faith and for valuable consideration from or through a creditor of the insolvent. In order to avoid a transfer it must be made out that the dominant motive of the transfer was to give preference to a creditor. The fact that a creditor is preferred is not enough (z). Thus payment made by a debtor on the eve of his insolvency to a creditor under

(s) Joy v. Campbell (1804), 1 Sch. & Lef. 328.

(t) Sec. 53; sec. 52 Prov. Ins. Act.

(u) Re Premlal Dhar, 44 Cal. 1016.

(v) Sec. 55 Pres. T. Ins. Act; sec. 53 Prov. Ins. Act.

(w) Off. Assignee v. Chettyar, 58 I.A. 115.

(x) Off. Assignee v. Palaniswami, 48 Mad.

740.

(y) Secs. 56-7; sec. 54 Prov. Ins. Act.

(z) Sharp v. Jackson (1899), A.C. 489.

pressure or under threat of legal proceedings, is not fraudulent preference. On the other hand, where a firm had become unable to pay its debts as they became due, and the agent of the firm transferred certain property and outstandings of the firm to a creditor who knew the position of the firm and had made a demand, it was held that the transfer was a fraudulent preference. A payment to a creditor to secure a benefit to the debtor himself, e.g. a fresh advance, or under the belief of a legal obligation to pay, is not within the section; so also payments made in the ordinary course of business. The onus of proving that there has been a fraudulent preference lies on the Official Assignee or the Receiver even if the debtor was insolvent at the time of the payment and knew himself to be so (a). Notice that fraudulent preference is voidable, not void. The jurisdiction of Insolvency Courts under this section also has been held to be exclusive. Where a transfer is set aside as fraudulent preference (e.g. under sec. 53 or 54 of the Provincial Act), it is only the share of the transferor (insolvent) which vests in the Receiver, not the share of others over which the insolvent had a disposing power (e.g. Hindu son) (a1).

Disclaimer of onerous property: Under sec. 62 of the Pres. Act, the Off. Ass. within 12 months of adjudication or 12 months of notice, is given power to disclaim (i.e. give up) in writing, any land with onerous covenants, shares and stock and other unproductive or unsaleable property belonging to the insolvent. On such disclaimer, all rights of the insolvent in the property will terminate from the date of the disclaim. Other parties' rights with regard to such property however are not to be affected by such disclaimer. As regards leaseholds, the Off. Ass. can disclaim only with leave of Court. Persons interested in disclaimed property can apply to Court for directions that such property should be delivered to them subject to such liabilities as the Court may decide. In case of leaseholds, the Court can order such delivery on the underlessee or mortgagee undertaking all the existing liabilities in respect thereof (e.g. for arrears of rent, performance of covenants, etc.). If the above parties refuse to accept the above conditions, the Court may grant such property to any person liable to perform the lessee's covenants under the lease (i.e. a co-lessee) and free from all incumbrances created by the insolvent (e.g. underlease or mortgage).

Dividends: After realising the property of the insolvent the Official Assignee shall with all convenient speed declare and distribute dividend among creditors who have proved their debts (c). (i) The first dividend (if any) shall be declared and distributed within one year of the adjudication, unless the Official Assignee satisfies the Court that there is sufficient cause for postponing the same to a later date. (ii) Subsequent dividends, in absence of reasons to the contrary, shall be declared and be payable at the interval of not more than 6 months. (iii) Before declaring dividends the Official Assignee shall cause notice of his intention to do so to be published in the prescribed manner and shall also send reasonable notice thereof to each creditor mentioned in the schedule who has not proved. (iv) After declaring dividend the Official Assignee shall send to each creditor who has proved, notice showing the amount of the dividend and how it is payable. He shall also send a statement of the estate of the insolvent if required by any creditor. (v) Where a partner in a firm is adjudged insolvent a joint creditor of the insolvent shall not receive dividend out of the separate estate of the insolvent until all separate creditors are paid in full out of his separate estate. (vi) In calculating dividend the Official Assignee shall retain sufficient assets in his hands to meet, (a) debts provable in insolvency and due to persons resident so far away that they have not had sufficient time to tender proof; (b) debts provable but not yet decided to be admissible; (c) disputed proofs and claims; (d) necessary expenses of the administration of the estate. Subject to the above, all moneys with the Official Assignee shall be distributed as dividends. Notice that where a proving creditor's name, through oversight, is not included in the list of creditors and a dividend is paid to the other creditors, the declaration is liable to be set aside and the excess of dividend received by the creditors who are paid will be ordered to be refunded. Note further that no lapse of time is bar to proof (d). (vii) A creditor who has not proved before the declaration of a dividend shall be entitled to be paid out of the money in the hands of the Official Assignee any

(a) *Sime Darby & Co. v. Off. Assignee*, 30 Bom. L.R. 290.

(a1) *Chenappa v. Off. Receiver*, A.I.R. (1955) Mad. 51.

(c) Secs. 69-76 Pres. T. Ins. Act; secs. 59-67 Prov. Ins. Act.

(d) *Re Mac Murdo* (1902), 2 Ch. 684.

dividend he may have failed to receive, before the money is applied in payment of future dividends, but he shall not be entitled to disturb any dividend declared before he proved his debts. (viii) When the estate is fully realised or so much of it is realised as the Official Assignee thinks proper without needlessly protracting the proceedings, the Official Assignee shall with the leave of the Court, declare a *final dividend*, but before doing so he shall give notice in the manner prescribed to all creditors who have not proved their claims, to the effect that if they do not prove their claims within the time mentioned therein he shall proceed to make the final dividend without regard to their claims. On the expiration of the time so limited or such further time as the Court may allow to any creditor the Official Assignee shall proceed to make a final dividend without regard to their claims. (ix) The Insolvent shall be entitled to any surplus remaining after payment in full of all his creditors with interest as provided by the Act and the expenses of the proceedings taken thereunder.

Limitation: The admission of a debt by the insolvent in his Schedule will extend the period of limitation, by way of acknowledgment. It has been held however that the Official Assignee is not entitled to pass an acknowledgment on behalf of the debtor nor is he an agent for the debtor for the purpose of keeping alive a debt due in insolvency (f).

Penalties: (i) An undischarged insolvent obtaining credit to the extent of Rs. 50 or upwards from any person without informing the person that he is an undischarged insolvent shall on conviction by a Magistrate be punishable with imprisonment which may extend to six months or fine or both. (ii) Any person adjudged insolvent who, (a) fraudulently with the intent to conceal the state of his affairs or to defeat the objects of the Act, (i) destroys or otherwise wilfully prevents or purposely withholds the production of any book, paper or other writing relating to such of his affairs as are subject to investigation or (ii) has kept or caused to be kept false books of account or (iii) has made false or withheld entries from or wilfully altered any book, paper or writing relating to the same or (b) fraudulently, with the intent to diminish the sum divisible amongst his creditors or of giving an undue preference to any of them, (i) has discharged or concealed any debt due to or from him or (ii) has made away with or charged, mortgaged or concealed any part of his property of whatever kind shall on conviction be punishable with imprisonment which may extend to two years. (iii) Where the insolvent has been guilty of any of the offences specified above, a discharge, or the acceptance or approval of a composition or scheme, shall not exempt him from being proceeded against in respect thereof (g).

Disqualifications of insolvent: Where a person is adjudged or readjudged insolvent, he shall, subject to the provisions of the Acts, be disqualified from: (i) being appointed or acting as Magistrate; (ii) being elected to any office of any local authority which is elective or to which no salary is attached; and (iii) being elected or sitting or voting as a member of any local authority. The disqualifications shall be removed (a) if the order of adjudication is annulled because he ought not to have been adjudged insolvent or because his debts have been paid in full, or (b) if he obtains from the Court an order of discharge, whether absolute or conditional, with a certificate that the insolvency was caused by misfortune, without any misconduct on his part. The Court may grant or refuse such certificate as it thinks fit (h).

Small insolvencies: Under the Pres. Act (i), where the Court is satisfied by affidavit or otherwise or where the Official Assignee reports to the Court, that the property of the insolvent is not likely to exceed *three thousand rupees* or such lesser sum as may be prescribed, the Court may make an order that the estate be administered in a summary manner and thereupon the provisions of the Act will apply with the following modifications: (i) no appeal shall lie from an order of the Court except with the leave of the Court; (ii) no examination of the insolvent shall be held except on the application of a creditor or the Official Assignee; (iii) the estate shall, if practicable, be distributed in a single dividend; (iv) such modifications may be made as may be prescribed with the view of saving expense or simplifying procedure. (v) Nothing however

(f) Carrimbai v. Ahmadali, 35 Bom. L.R. 12.

(g) Secs. 102-105 Pres. T. Ins. Act; sec. 72 Prov. Ins. Act.

(h) Sec. 103 Pres. T. Ins. Act; sec. 73 Prov. Ins. Act.

(i) Sec. 106.

shall permit modification of the provisions of the Act relating to discharge. (vi) The Court may, at any time, if it thinks fit, revoke an order for summary administration. Similar provisions are made by the Prov. Act (j), except that, under the latter Act, the debtor is bound to apply for his discharge within 6 months of his adjudication.

Administration of estate of deceased insolvents: Under the Pres. Act (k), (i) any creditor of a deceased insolvent whose debt would have been sufficient to support an insolvency petition against the debtor, if he had been alive, may present to the Court within whose local limits the debtor resided, or carried on business for the greater part of six months immediately prior to his decease, a petition for administration of the estate of the deceased insolvent under the Act. (ii) After giving the prescribed notice to the legal representatives of the deceased debtor, the Court may, on proof of the petitioning creditor's debt, and if not satisfied that the estate will be sufficient to meet all the debts, make an order for the administration of the estate of the debtor in insolvency. The Court may, upon cause shown, dismiss the petition also. (iii) A petition under the sec. shall not be presented when administration proceedings are already pending in a Court of law with regard to the same estate, but such latter Court shall, in such case, on proof that the estate is not sufficient to pay all the debts, transfer the proceedings to the Court exercising insolvency jurisdiction and such Court may make an order for administration of the estate in insolvency. (iv) On an order being made for administration as above, the property of the insolvent shall vest in the Official Assignee and he shall forthwith proceed to realise and distribute the same in accordance with the provisions of the Act. All the provisions of the Act with regard to the administration of the property of the insolvent shall, except as noticed below, apply as far as practicable, to administration under the above section. (v) The Official Assignee, in administration under sec. 108, shall have regard to any claim by the legal representative of the deceased debtor to payment of proper funeral and testamentary expenses incurred by him in or about the debtor's estate. This claim will be preferential claim and shall be paid in full out of the debtor's estate in priority to all other debts. (vi) If any surplus remains in the hands of the Official Assignee after paying in full all debts due together with costs and interest as provided by the Act, the same shall be handed over to the legal representative of the deceased debtor or otherwise as may be prescribed. (vii) After notice of the presentation of a petition under sec. 108, no payment or transfer of property made by legal representative shall operate as a discharge to him as between him and the Official Assignee. Save as above, nothing in secs. 108-109, however, invalidates any payment made or act done in good faith by the legal representative or by a District Judge under sec. 64 of the Administrator-General's Act, before the date of the order of administration. (viii) The above provisions shall not apply where letters of administration to the estate of a deceased debtor have been granted to the Administrator-General.

Unclaimed dividends: Where the Official Assignee has in his hands dividends which have not been claimed for 15 years, or such less period as may be prescribed, he shall pay them over to the credit of the Government of India unless the Court otherwise directs. Any person claiming thereafter the said dividends may apply to the Court and the Court, after a month's notice to show cause to any officer the Government may appoint in this behalf, and if satisfied as to the claim, may make an order of payment to him of the sum due (l).

CHAPTER XVII

ARBITRATION

Application of the Act: The law as to arbitration is now contained in the Arbitration Act of 1940 (Act X of 1940), which applies to the whole of India. Before this Act was passed, the law was contained partly in the 2nd Schedule to the Civil Procedure Code and partly in the Arbitration Act of 1899. These are now repealed.

(j) Sec. 74.
(k) Secs. 108-111.

(l) Secs. 112-13, Pres. T. Ins. Act.

The Act applies (i) to arbitration without the intervention of Court (ii) to arbitration through Court, where no suit is pending and (iii) to arbitration in suits. In fact it applies to all arbitrations (sec. 47) including statutory arbitrations (sec. 46). The rules laid down by the Act are binding upon the Crown also (sec. 45). The object of arbitration is to substitute a domestic tribunal for adjudication of disputes in place of the Law Courts. Once such a tribunal reaches a final decision, the Act operates to put the decision into effect (m).

Arbitration Agreement: This is defined to mean "a written agreement to submit present or future differences to arbitration, whether an arbitrator is named therein or not" (sec. 2). Such an agreement, therefore, in order to be valid, requires *three conditions* to be fulfilled:

(i) It must be in writing, i.e. there can be no oral submission to arbitration. This does not mean that there must in each case be a formal submission paper properly signed by the parties to the dispute. No particular form is necessary. What is required is a written agreement between the parties, agreeing to go to arbitration with regard to particular disputes which have arisen or which may hereafter arise. The writing need not be signed by the parties. It is enough if it is accepted by the parties as binding. In a Bombay case (n), the rules and regulations of an Exchange, which contained provision for reference of disputes between members and members to arbitration, were held to be sufficient to bind the members of the Exchange between whom disputes had arisen, to go to arbitration as directed therein. The bye-law of an association of which parties are members, viz. that "only after obtaining an award from arbitrators, can any party go to a Court of Law to obtain relief in respect of any transaction", may amount in law to an "agreement in writing to refer disputes to arbitration" (n1). It is not necessary to constitute an arbitration agreement in writing that a writing should be signed by both parties. It is enough if the terms are reduced to writing and the agreement of the parties thereto is established (n2). Arbitration agreement should state definitely the person or persons to whose arbitration the dispute is to be referred. The arbitration agreement to refer to X or Y is bad for uncertainty. An agreement however to refer to X and at the option of one of the parties to Y, is not void for uncertainty (n3).

(ii) There must also be a present or future dispute, which is intended to be covered by the agreement. Arbitration presupposes the existence or the possible existence of a dispute. If there is no dispute between the parties, the agreement will not operate. Thus where a demand was made by a creditor on the debtor to pay the amount due, to which the debtor sent no reply, a suit to enforce payment was held in order, though the transaction out of which the debt arose contained an arbitration cl. (o). Any dispute however is enough, e.g. taking of partnership accounts, a counter-claim or a claim for set-off (p).

(iii) The dispute must be one which is covered by the arbitration agreement. This is, of course, a question of construction. Notice however that if the contract containing the arbitration cl. is itself challenged by a party, e.g. as not binding, there will be no scope for the arbitration cl. to operate (q). On the other hand, a dispute resulting from or arising out of an admitted contract, which contains an arbitration cl., e.g. a broker's closing of an original transaction, on the constituent's failure to provide margin, will be covered by the cl. (r).

It has been held by the Supreme Court (s) recently that where the arbitration cl. provides that "all matters, questions, disputes, differences and/or claims arising out of

(m) Fazalalli v. Khimji, 36 Bom. L.R. 1005.

(n) Chinniram v. Vandrawandas, 49 Bom. L.R. 431.

(n1) Prataprai v. M/s. Shiva Narayan & Co., A.I.R. (1956) Bom. 97.

(n2) Jugalkishore v. Goolbai, A.I.R. (1955) S.C. 812.

(n3) Laxmichand v. Kishanlal, A.I.R. (1955) Cal. 588.

(o) Dawoodbhai v. Abdul Kader, 33 Bom. L.R. 51.

(p) Uttamchand v. Jeeva, 46 Cal. 434.

(q) Mahomed v. Pirojshaw, 34 Bom. L.R. 697.

(r) Sukhanand v. Maneklal, 42 Bom. L.R. 1135.

(s) A. M. Mair & Co. v. Gordhandas, A.I.R. (1951) S.C. 9.

and/or concerning and/or in connection with and/or in consequence of or relating to" the contract should be referred to arbitration a dispute whether the time of performance was extended and further whether a party to the contract was acting as agent of another or as principal, was covered by the words of the cl. An agreement to refer all matters in disputes "in relation to the contract" or "in connection with the contract" or "regarding the contract" would include a dispute whether the contract came to an end by frustration or recession or by breach of condition or was avoided by reason of fraud, misrepresentation or coercion. It would be otherwise if the dispute was whether the parties were *ad idem* at all (t). A contract may come to an end, e.g. by frustration, but the arbitration agreement may remain operative. Similarly, the arbitration agreement may be declared void without the contract being declared invalid. The test whether the arbitration agreement falls with the contract is whether the contract is determined by something outside itself (in which case the arbitration clause is determined with it) or by something arising out of the contract (in which case the arbitration clause remains valid and can be enforced) (u).

Submission paper: This is no longer necessary, though it is always advisable to get the parties to sign a submission paper clearly defining (i) the names of the arbitrators, (ii) the matters which are referred to them for arbitration, (iii) the powers which they are to exercise and (iv) the procedure which is to be followed if they differ.

Appointment of arbitrators: Generally, the "arbitration agreement" mentions the names of the arbitrators. They may be one or more than one, i.e. two, three or more. If the arbitration agreement fails to mention their number, the reference shall, under the First Schedule to the Act, be to a single arbitrator (sec. 3). The parties may agree that any named third person may appoint the arbitrator or arbitrators (sec. 4).

Appointment of umpire: Under cl. 2 of Sch. I, where the reference is to an even number of arbitrators, they shall appoint an umpire at the latest, within one month of their respective appointments, unless the agreement otherwise provides. Under sec. 8, the Court also has power to appoint an umpire where (i) the parties or the arbitrators, having the power to do so, do not appoint an umpire or (ii) where the appointed umpire neglects or refuses to act or becomes incapable of acting or dies and the parties or the arbitrators do not supply the vacancy.

Who can appoint an arbitrator: Any person competent to contract can appoint an arbitrator. A minor cannot appoint one nor can a natural guardian of a minor (v). A certified guardian however can make such a reference, with leave of the Court (w). The Karta (manager) of a joint Hindu family, e.g. the father, can bind his minor sons by a reference to arbitration (x). A partner has no implied power to refer a partnership dispute to arbitration (y).

Reference to three arbitrators: Notice that where reference is to three arbitrators, one to be appointed by each party, and the third to be appointed by the two arbitrators, the agreement shall be construed as if it provided for the appointment of an umpire, instead of a third arbitrator (sec. 10). In cases other than the above, where a reference is to three or more arbitrators, the opinion of the majority shall prevail (unless the agreement provides otherwise). If they are equally divided, the opinion of the umpire shall prevail (with the same qualification) (sec. 10, cls. 2, 3).

Power of Court to appoint arbitrator or umpire: Where (i) the parties to the arbitration have to appoint an arbitrator or arbitrators by consent, but they do not all concur in the appointment; (ii) where the appointed arbitrator, or umpire, neglects or refuses to act, or becomes incapable of acting or dies, and the parties or the arbitrators do not supply the vacancy or (iii) where the parties or the arbitrators do not appoint

(t) *Tolaram v. Birla Jute Manuf. Co. Ltd.* (1948), 2 Cal. 171.

(u) *State of Bombay v. Adamje, A.I.R.* (1951) Cal. 147.

(v) *Har Narayan v. Saggan Pal*, 67 I.A. 386.

(w) *Samadkhan v. Ramzan Khan, A.I.R.* 1938 Lah. 582.

(x) *Ramchwar v. Ram Bahadur*, 34 Cal. 70.

(y) Sec. 19, Partnership Act.

an umpire, the Court may appoint such arbitrator or umpire (sec. 8). A "Sar Panch" does not necessarily mean an "Umpire". He has position akin to Chairman (y1).

The procedure is for a party to give written notice to the other parties, calling upon them to make the necessary appointment. If within 15 clear days thereafter, no such appointment is made, the party may apply to Court and the Court, after hearing the other parties, may make such order on the application as it thinks fit (ibid). The Court can exercise its power under the sec. even where the reference is to more than two arbitrators.

(iv) Where the Court removes an arbitrator or umpire under sec. 12 (see seq.), the Court may also fill up the vacancy. (v) Where the authority of an umpire or an arbitrator or arbitrators is revoked under sec. 5, the Court may also appoint a person to be the sole arbitrator. It may also, in such case, supersede the reference altogether (sec. 12, cl. 2).

Power of a party to appoint new or sole arbitrator: (i) Where the agreement provides for a reference to two arbitrators, one to be appointed by each party, and either of the appointed arbitrators neglects or refuses to act, or becomes incapable of acting or dies, the party appointing him may appoint a new arbitrator in his place. (ii) If one party, either originally or by way of substitution as above, fails to appoint an arbitrator within 15 days after written notice to do so by the other party, such latter party may appoint his own arbitrator the sole arbitrator, and his award shall thereupon be binding on both the parties, as if he was appointed by consent (sec. 9). (iii) The Court, however, in the second case, may set aside such appointment and may give further time for the appointment of the second arbitrator or may make such other order as may seem just.

Who may be appointed arbitrator: Any person competent to contract can act as arbitrator. An association or a panel of some of its members, as fixed by its rules, e.g. East India Cotton Association, can also act as such. A particular Court, e.g. an English Court, or a particular Judge, e.g. a Judge hearing a matter, may also be appointed as arbitrator.

Arbitrator's authority irrevocable: Once arbitrators are duly appointed, their authority to act as such cannot be revoked by the parties subsequently, unless the arbitration agreement otherwise provides. Only a Court's order, superseding the arbitration, can have such effect (sec. 5).

The Court will supersede the arbitration if the arbitrator misconducts himself, or acts fraudulently or is guilty of unreasonable delay or if any other just and sufficient cause is shown. Notice that the agreement is not revoked by the death of a party to arbitration (sec. 6) nor by his insolvency, if the Official Assignee elects to adopt the agreement (sec. 7).

Revoking authority of arbitrator: Under sec. (5), two principles are to be followed in exercising jurisdiction: (i) the Court should not lightly release parties from their bargain to go to arbitration, and (ii) the Court should be satisfied that substantial miscarriage of justice will take place unless authority is revoked (z).

Removal of arbitrator or umpire by Court: On the application of a party to the reference, the Court may remove an arbitrator or umpire if (i) he fails to use all reasonable diligence in entering upon, or proceeding with the reference or in making the award or (ii) if he misconducts himself or (iii) if he misconducts the proceedings (sec. 11). An arbitrator or umpire so removed, is not entitled to any remuneration (ibid).

As regards (i), notice that arbitrators must make their award within 4 months of their entering on the reference, if the agreement does not fix any particular time-limit for making the award (cl. 4, Sch. I). They have no right to extend the time fixed for making the award, except with the consent of all the parties (sec. 28). Similarly, an

(y1) Chauthmal v. Ramchandra (1955)
Nag. 100.

(z) Bhuwalka Bros. v. Fatechand, A.I.R.
(1952) Cal. 294.

umpire must make his award within 2 months of entering on the reference unless the agreement fixes the time (cl. 5, Sch. I).

As to (ii) and (iii), notice that the first covers cases of moral turpitude on the part of the arbitrator or umpire, while (iii) covers cases of what is called "*legal or judicial misconduct*", i.e. failure, however innocent, on the part of the arbitrator to observe the duties and responsibilities of his office (a). Instances of (ii) are: corruption, fraud or partiality on the part of the arbitrator during the course of the proceedings or his being disqualified to act as such. Instances of (iii) are: admitting inadmissible evidence, calling a witness whom no party has called (b), unreasonable delay in proceeding with the reference or the arbitrator being found to have a secret interest in the subject-matter of the reference. In all the above cases, the Court, on such removal, may (i) appoint a person or persons to fill up the vacancy or (ii) appoint a person to act as sole arbitrator or (iii) supersede the reference altogether (sec. 12).

Powers of arbitrator or umpire (sec. 13): Subject to any provision to the contrary, an arbitrator or umpire has power (i) to administer oaths to parties and witnesses, (ii) to state a point of law as a special case for opinion of Court or state the award in the form of a special case for the opinion of the Court, (iii) to make a conditional or alternative award, (iv) to correct any clerical mistake or omission and (v) to administer such interrogatories to the parties as may be necessary. Arbitrators are not circumscribed in their jurisdiction as a Court of Law is. They have no territorial bounds and they can divide property, wherever situate, all over the world (b1).

Notice that under the Indian Act there is no provision, as there is under the English Act, to compel an arbitrator to state a case for the opinion of the Court. To these powers may be added, (vi) the power to make interim award (sec. 27), (vii) to award interest, and (viii) to award costs and to tax the same (cl. 8, Sch. I).

Hearing of the reference: An arbitrator is not bound to follow all the technical rules of law and procedure while hearing the reference, provided he does not violate principles of natural justice (c). He must hear both sides, and in the presence of each other. He must allow proper cross-examination of witnesses produced. Proper notices of all meetings should be given to the parties. *Ex parte* hearing without just cause will be "legal misconduct". He has power to order discovery and inspection of documents (cl. 6, Sch. I). He can also serve interrogatories (sec. 13). He can admit or exclude evidence, according as the order of reference justifies his doing so. He cannot import his own knowledge in deciding the reference, unless he is appointed as an expert arbitrator in a commercial dispute (d). Where more than one arbitrator is appointed, all the arbitrators must act together at every stage of the proceedings and they must all be present throughout the reference when important decisions are taken. If an arbitrator refuses to act, while the reference is pending, an award by the rest would be bad. Before closing the reference, notice of the arbitrators' intention to do so must be given to the parties. If the arbitrators disagree and give to any party to the reference or to the umpire, a written notice as to the same, or if the arbitrators allow their time to expire without making any award, the umpire shall forthwith enter on the reference in their place and stead (cl. 4, Sch. I).

Effect of order of reference: Once the suit is referred to arbitration as above, the Court's powers are curtailed. It cannot deal with the subject of the reference till the reference is revoked (sec. 23). It can only act in a supervising capacity. The arbitrator appointed under the order of reference is not an officer of the Court; he acts as any private arbitrator, and he is bound to conduct the arbitration as such. The Court can again become seized of the subject-matter only (i) if by order it supersedes to arbitration or (ii) if an award is made and filed in Court, when the Court can proceed to deal with matters arising out of the award.

(a) Gangasahai v. Lekhraj, 9 All. 253.

(b) Re Enoch etc. Co. (1910), 1 K.B. 327.

(b1) Chauthmal v. Ramchandra (1955) Nag. 100.

(c) Municipality of Ahmedabad v. Ravji-bhai, 59 Bom. 268.

(d) Rattansi v. Bombay United etc. Co., 41 Bom. 578.

Notice however that under sec. 41, the Court is given certain powers to grant interim reliefs while arbitration proceedings are pending. These powers are: (i) to pass orders for the preservation, custody or sale of any goods to which the reference relates; (ii) for securing the inspection of subject of dispute and for taking samples therefrom or conducting any experiment with reference thereto; (iii) for interim injunction and receiver; and (iv) for appointing guardians of minor and insane parties to a reference (Sch. II). The Court has also power to issue processes to parties and witnesses whom the arbitrator or umpire wishes to examine (sec. 48).

Time for making the award: Unless the agreement otherwise provides, arbitrators are bound to make their award within four months *after entering upon the reference* or after written notice from a party calling upon them to act, or within such time as the Court may allow (cl. 3, Sch. I). The Court may, if it thinks fit, and whether the time for making the award has passed or not, and whether the award has been made or not, extend the period (sec. 28). No provision in the arbitration agreement, empowering the arbitrators to extend time for making the award, except by consent of all parties, shall be valid (*ibid*). An umpire shall, unless the agreement otherwise provides, make his award within two months of his entering on the reference or within such extended time as the Court may allow (cl. 5, Sch. I). An arbitrator cannot be said to have "entered on a reference" as soon as he accepts the position of arbitrator. He must have done some overt act as arbitrator, e.g. hold a preliminary meeting and give directions as to how the arbitration is to proceed (*d1*).

Making the award (sec. 14): When the arbitrator or the umpire has made his award, he must sign it and give notice in writing to the parties of the same. He may also inform them of the fees and charges payable by them in respect of the arbitration. He is however not bound to file the award in Court. He will do so only if (i) any of the parties to the arbitration requests him or (ii) if the Court orders him to do so, and in either case (iii) upon payment to him of the fees and charges payable in respect of the arbitration and the award and the costs of filing the award in Court. This is because the arbitrator has a lien on the award for these charges. If these conditions are fulfilled, he is bound to file the award or a signed copy thereof in Court, together with all depositions taken before him and all documents filed before him during the proceedings. On such filing of the award in Court, the Court will give notice of the fact to the parties. In case the arbitrator has submitted a special case for the opinion of the Court, the Court, after hearing parties, shall give its opinion thereon which shall then form part of the award.

Notice that after an award is made, the arbitrator becomes *functus officio* and his authority is not revived, even if the award is subsequently set aside. Notice further that an award made on a reference to arbitration in a pending suit, outside the Court, can now, with the consent of all parties, be recorded as a compromise of the suit under sec. 47.

Powers of the Court re: award (secs. 15-19)

After the award is filed as above, the Court has the following powers: (i) to modify the award in certain cases (sec. 15); (ii) to remit it to the arbitrators for reconsideration (sec. 16); (iii) to set it aside on proper grounds (secs. 19, 30) or (iv) to pass a decree in terms thereof (sec. 17). (v) The Court may, in fit cases, after the award is filed and before notice of the fact has been given to the parties, pass such interim orders as the justice of the case may require (sec. 18).

As to (i), the Court may modify an award, if (a) a part of it, provided it is separable, is on a matter which was not referred to arbitration; (b) if the award is imperfect in form or contains an obvious error, which can be corrected without affecting the decision or (c) if it contains a clerical mistake or accidental omission (sec. 14).

As to (ii), the Court may remit the award to the arbitrator for reconsideration if (a) it omits to determine any matter which falls within the reference; (b) if it determines matters not referred to arbitration and such matters cannot be separated from

those which are referred; (c) if the award is so indefinite as to be incapable of execution and (d) if there is an objection to the legality of the award, *which is apparent on the face of it* (sec. 16). "Error appearing on face of award" includes a case where there is no evidence before the arbitrators to support their findings. In determining whether there is an "error on the face of the record" a distinction must be drawn between cases in which a question of law has been specifically referred to the arbitrators and cases in which a question of law arises incidentally in course of arbitration. In the first case, the Court will not interfere, even if the arbitrator's decision is wrong. In the latter case, there is scope for the Court to interfere, if it is of opinion that the arbitrator has acted illegally in reaching his decision, e.g. if inadmissible evidence is admitted, or if a principle of construction has been adopted by him which the law does not countenance or something of a similar nature (d2). The Court will fix the time within which the arbitrator, on such remission, shall submit his decision to Court. The Court may extend such time also, if necessary. If the award is not made within the time so fixed, it shall be regarded as void. As to (d), notice that an award cannot be remitted for reconsideration because the Court thinks that the arbitrators' decision was wrong. Even an error of law does not vitiate an award (e). It is only if the award on the face of it shows a patent error of law, e.g. a clear misconstruction of a bye-law (f), that the Court will remit the award. As regards (iii) and (iv), see seq. Where the award is a nullity, it cannot be referred back to the arbitrator under the sec., e.g. where the arbitrators have not acted jointly (f1). The Court has power to extend time, when award is remitted for reconsideration (f2).

Decree in terms of award (sec. 17): If the Court sees no reason to remit the award, or set it aside, it will pronounce judgment in terms of the award, after the time to file an application to set aside the award has passed or if such application is made, after it is refused. Upon such judgment, a decree shall follow. The decree so passed will not be subject to appeal except on two grounds: (i) that it is in excess of the award or (ii) is not in accordance therewith. This is because the law always wishes to give finality to awards. The period for appeal from an award is 30 days from service of notice of filing the award in Court. Notice that a decree passed on an award without allowing the requisite time to elapse is a nullity and can be set aside (g).

Setting aside an award (secs. 19, 30)

An award can be set aside if

- (i) the arbitrator or umpire has misconducted himself; or
- (ii) has misconducted the proceedings;
- (iii) where the award has been made after an order of the Court superseding the arbitration;
- (iv) where it has been made after the arbitrators have notice of commencement of legal proceedings between all the parties to the reference, with regard to the whole subject-matter of the reference (sec. 35);
- (v) if the award is improperly procured; or
- (vi) if it is otherwise invalid. Except on these grounds, an award cannot be set aside.

As to (i), the cl. is intended to cover cases where the arbitrator has been guilty of fraud or other malpractices, e.g. taking improper gratification from a party. Bias or partiality towards a party, if strictly proved, is also within the cl. Existence of or acquisition of personal interest in the subject of the reference without the knowledge of the parties is also a ground of disqualification under the cl. (h).

(d2) Thaverdas v. Union of India, A.I.R. (1955) S.C. 468.

(e) Pestonji v. Jaisingdas, 21 Bom. L.R. 420.

(f) Mcenakshi Mills v. Langley & Co., 58 Bom. 288.

(f1) Haran Chandra v. Krishna Kant, A.I.R. (1955) Ass. 61.

(f2) Ganapatrai v. Ram Gopal, 59 C.W.N. 607.

(g) Shaikh Esuf v. Shaikh Dawood (1951), 1 Mad. L.J. 193; Ganeshmal v. Keshoram Cotton Mills, 55 C.W.N. 349.

(h) British Corporation v. John Arid & Co. (1913), A.C. 241.

Cl. (ii) refers to cases of "legal misconduct", i.e. conduct which, though not involving moral turpitude, is still so substantially unfair that the Court will not allow the award to be valid and binding. This is because the arbitrators occupy a quasi-judicial position. Thus if an arbitrator has not followed rules of natural justice while conducting the proceedings, e.g. has heard parties in absence of each other, has not allowed a party to be heard at all or lead his evidence, has refused a necessary adjournment, in all such cases the award will be set aside. Of course, an arbitrator is not bound by the technical rules of evidence or procedure (i) but if such irregularities amount to not properly hearing the case at all, it would amount to "legal misconduct" (j).

Assessing damages at black-market prices, substituting a third party's views as to amount of damages to their own, or basing a finding on no evidence, refusing to record evidence when tendered, where evidence is required to be taken (k), asking for information from third parties without the knowledge or consent of the parties concerned (l), is "misconduct".

An arbitrator is bound to disclose to the parties all circumstances and facts which are calculated or likely to influence his judgment and bias his mind in favour of one party or the other. He must show "ubberima fides" to the parties whose disputes he is going to adjudicate and who have constituted him their domestic forum. If he fails to do so, he is guilty to judicial misconduct and the award can be set aside on that ground (m).

If the award does not decide all questions in dispute but adjudicates the claim of one party only and not that of the other, the award is invalid and cannot be filed and enforced. An award passed by an arbitrator in direct contravention of his findings is illegal on the face of it and will be set aside (n). Though arbitrators who are experts in trade can decide a matter within their knowledge, without evidence, a finding by arbitrators, e.g. as to extension of time of performance, based upon no evidence will clearly amount to legal misconduct (o). Where under the arbitration clause the dispute was to be referred to Bengal Chamber of Commerce whose rules empowered the Chamber to decide on statements filed by parties before them, held, an award made on such statement without calling further evidence was not bad (o). Award granting damages on a wrong basis is bad on the face of it and will be set aside (o). An arbitrator asking for fees from one party and threatening that he will not proceed till they are paid is not guilty of misconduct (ol). The Court has power under sec. 30 to set aside an award on the ground of patent illegality. As regards the exercise of this power, no question of limitation can arise (p).

As to Cl. (iv), notice that arbitrators do not now become *functus officio* as soon as a suit is filed between the parties relating to the subject-matter of arbitration. It is necessary that (i) the suit or legal proceedings should be with regard to the whole of the subject-matter of reference, (ii) notice of the suit must have been given to the arbitrators or the umpire, and (iii) it is only further proceedings after such notice that are made invalid (q).

Cl. (v) refers to cases where either party has been guilty of fraudulent concealment of any matter which ought to have been disclosed to the arbitrators or wilfully misleading or deceiving the arbitrators.

Cl. (vi) is general in expression. It has been invoked to attack an award on the ground of want of jurisdiction (r) as also on the ground that the order of reference itself was invalid (s). Thus if the award is in excess of the matters referred to the

(i) Harising v. Kankinara Co. Ltd., 34 C.L.J. 39.

(j) Amir Begum v. Badruddin, 36 All. 336.

(k) Bajranglal v. Ganesh Commercial Co. Ltd., 55 C.W.N. 147.

(l) Hysien v. Kesardeo, 92 C.L.J. 224.

(m) Satyendra Kumar v. Hind Construction, 54 Bom. L.R. 37.

(n) Maruti v. Akram, 49 Bom. L.R. 294.

(o) Bijoyising v. Bilasroy & Co., A.I.R. (1952) Cal. 440.

(ol) Teja Sing v. Union of India, A.I.R. (1955) All. 566.

(p) Hastimal v. Hiralal, 56 Bom. L.R. 99.

(q) Re All India Groundnut Syndicate, 47 Bom. L.R. 420.

(r) Lakshmi Narayan v. Ramchandra, 34 M.L.J. 71.

(s) Mahomed v. Valli, 26 Bom. L.R. 171.

arbitrators, if it is out of time, if it is bad for want of registration, if the appointment of the arbitrators or the umpire was invalid or if the contract containing the arbitration cl. itself turns out to be void, the award can be attacked under this cl.

Notice that once an award is made, no suit can be filed to set aside the award (sec. 32) nor can the decree be attacked except on the two grounds mentioned in sec. 21. The Court while setting aside an award, may, if it thinks fit, supersede the arbitration also (sec. 19).

Arbitration through Court (sec. 20): The parties to an arbitration agreement may, instead of proceeding thereon privately, have the agreement made a rule of the Court, so that thereafter, the Court becomes seized of the matter. The procedure is (i) for all or some of the parties to apply to the Court having jurisdiction to file the agreement; (ii) the application on being filed, will be numbered and registered as a suit; (iii) the Court shall direct notice of the application to be given to the other parties to the agreement, directing them to show cause why the agreement should not be filed. (iv) If no sufficient cause is shown, the Court shall order the agreement to be filed and shall thereupon refer the matter to the arbitrator appointed by or agreed to by the parties or in absence of such agreement, to one appointed by the Court. (v) Thereafter the arbitration shall proceed in accordance with the provisions of the Act, so far as they are applicable. The parties, by this procedure, save the expenses of a suit and at the same time, have the arbitration proceedings conducted under the supervision of the Court.

Arbitration in pending suits (secs. 21-25): Where all the parties interested in a suit agree that any matter in difference in the suit shall be referred to arbitration they may: (i) before judgment is pronounced, apply to the Court (ii) in writing, for an order of reference (sec. 21). Where some only of the parties to a suit, desire such a reference, the application shall be made by such parties, on which the Court will order a reference to be made; and the award made on such reference shall be binding on these parties only. As regards the other parties, the suit shall proceed, as if no order of reference has been made (sec. 24). On a reference order being made as above, the arbitrator shall be appointed in such manner as may be agreed upon between the parties (sec. 22). The Court, by the order of reference, shall also fix the time within which the arbitrator is to make his award (sec. 23). All the other provisions of the Act, so far as they are applicable, shall apply to such arbitration (sec. 24), (viz. powers of Court to appoint an umpire under sec. 8, powers of Court to remove arbitrator under secs. 11 and 12, powers to modify, or remit the award or to set it aside under secs. 15, 16, 19 and 30), except that instead of exercising powers of filling up vacancies and making new appointments of arbitrators or umpire under secs. 8, 10, 11 and 12, the Court may, in case of such arbitrations, supersede the arbitration altogether and proceed with the suit (sec. 25).

It has been recently held in Calcutta that a reference to arbitration, while a suit is pending, without an order of reference by the Court, is invalid, and an award made on such arbitration cannot be filed or enforced. If however all the parties to the suit, subsequently agree before the Court, that the Court should record the award as a compromise or adjustment under O. 23 of the Civil Procedure Code, the Court is bound to do so. The Madras High Court has also taken the same view (t).

Where reference to arbitration is through Court, the powers of the arbitrator as defined by the Court cannot be extended by the parties by consent. They must obtain the Court's order to enlarge the powers first (u).

Jurisdiction (sec. 31): An award can be filed in any Court which has jurisdiction over the matter which is the subject of the reference (ibid). The Act further provides that all questions regarding the validity, effect or existence of an award or an arbitration agreement, arising between parties thereto, or those claiming under them, shall be decided by the said Court and by no other. Similarly, all applications regarding the conduct of arbitration proceedings or arising thereout, shall be made to the same Court and to no other. If an order on an application under the Act has been made in a Court competent

(t) Abdul Rehman v. Mahomed, A.I.R. (1935) Mad. 781 F.B.; Jugaldas v. Parshotam, 92 C.L.J. 181.

(u) Sherbanoo v. Hoosenbhai, 50 Bom. L.R. 89.

to entertain it, that Court alone shall have jurisdiction over the arbitration proceedings and all applications arising thereout (ibid). Thus no suit can be filed to set aside an arbitration agreement (v).

Procedure (sec. 32): Notice that under the Act, no suit can lie on any ground whatsoever, for decision of the question of the existence, effect or validity of an arbitration agreement or award, nor can either of these be set aside amended, modified or otherwise affected otherwise than as provided by the Act (ibid). However, the award must, within time, be filed in Court as provided by sec. 32 and becomes operative only on being made a rule of the Court (w). When a party to an arbitration agreement desires to challenge the existence or validity of an arbitration agreement or an award or to have the effect of either determined by the Court, he must apply to the Court, which will then determine the matter either on affidavits or by taking evidence as in a regular suit (sec. 33). Thus no suit can now be filed to set aside an award on the ground that it is invalid, nor can the invalidity of an award be made a defence to a suit on the award. The party must, in such a case, proceed by an application under sec. 33. A suit to set aside an arbitration agreement (and award made thereon) on the ground that the party was induced to enter into the agreement by reason of fraud is not maintainable in view of sec. 33 (x). Similarly, a suit to enforce an award is not now maintainable in view of sec. 32 (y). A suit for a declaration that a contract containing an arbitration clause was never entered into is maintainable (z).

Effect of legal proceedings on arbitration (sec. 35): No reference or award becomes invalid merely because a party to the reference has started legal proceedings as regards the subject-matter of the reference, but where legal proceedings (i) covering the whole subject-matter of the reference have been started (ii) between all the parties to the reference and (iii) notice thereof is given to the arbitrators or umpire, all further proceedings in the reference thereafter will be invalid unless (iv) a stay of the suit is granted as stated below (ibid). Notice that arbitrators do not now become *functus officio* as soon as a suit is filed between the parties relating to the subject-matter of arbitration. It is necessary that (i) the suit or legal proceedings should be with regard to the whole of the subject-matter of reference, (ii) notice of the suit must have been given to the arbitrators or the umpire, and (iii) it is only further proceedings after such notice that are made invalid (z1).

Stay of suit (sec. 34): Where a party to an arbitration agreement, or a person claiming under him files a suit in a Court of law against the other party with respect to any matter which is covered by the arbitration agreement, the latter party may, before filing his written statement or taking any other step in the proceedings, apply to the Court to stay the proceedings. The Court on such application, may stay the proceedings, if satisfied (i) that there is no sufficient reason why the matter should not be referred to arbitration and (ii) that the party applying has been always and is then ready and willing to go to arbitration (ibid).

Three conditions must be satisfied before a Court will order a stay of suit regarding a matter covered by the arbitration agreement: (i) the party asking for stay must have applied at the earliest opportunity, e.g. before filing his written statement and before taking any other step in the proceedings; (ii) there must be no sufficient reason against the reference and (iii) the party applying must have been ready and willing, at all material times, to go on with the reference. As to (i), "taking a step in the proceedings" has been held not to include filing an appearance in the suit (a) or signing a consent decree for adjournment (b). Taking out a summons for particulars or for

(v) *Bhagwansing v. Atmasing*, 47 Bom. L.R. 716.

(w) *Kishori v. Bhairavi Nandan*, A.I.R. (1953) Pat. 42.

(x) *Seethamma v. Annappauranamma* (1952), 2 Mad. L.J. 744.

(y) *Narbadabai v. Natvarlal*, 55 Bom. L.R. 408.

(z) *State of Bombay v. Adamjee Dawood & Co. Ltd.*, A.I.R. (1951) Cal. 147.

(z1) *Re All India Groundnut Syndicate*, 47 Bom. L.R. 420.

(a) *Bhawanidas v. Pannachand*, 52 Cal. 453; *Nuruddin v. Abu Ahmad*, 51 Bom. L.R. 410.

(b) *Chimanram v. Vandravandas*, 49 Bom. L.R. 431.

discovery and inspection however or applying for security for costs would amount to "a step in the proceedings" (c). As to (ii), where charges of fraud are made or where difficult questions of law are likely to arise, these have been held to be sufficient reason for the Court not ordering a stay of suit (d).

Where arbitration condition precedent (sec. 36): Where an agreement provides that in case of disputes an award of an arbitrator shall be a condition precedent to the right of a party to file a suit in a Court of law, with regard to the subject-matter of the dispute, such an agreement is not *ipso facto* invalid. In such a case, however, the Court, if it decides that the agreement shall cease to apply to a particular difference, has also the power to hold that the above cl. (of compulsory arbitration) shall not apply to that difference (ibid).

Limitation (sec. 37)

All the provisions of the Limitation Act apply to arbitration proceedings also. Notice however that where an award is set aside, or where the Court orders that the arbitration agreement shall cease to have effect with regard to a particular difference which is being arbitrated upon, the period between the commencement of the arbitration and the date of the Court's order must be excluded in computing the period of limitation (ibid). For the purposes of limitation an arbitration is deemed to have commenced when one party thereto serves a notice on the other party requiring the appointment of an arbitrator or requiring the difference to be referred to the named person in the arbitration agreement for adjudication.

Similarly, where an arbitration agreement provides that any claim to which the agreement relates shall be barred unless notice to appoint an arbitrator is given or an arbitrator appointed, or some other step is taken to commence arbitration proceedings within a certain time, the Court has power to extend such time, if in its opinion, undue hardship is likely to be caused otherwise. Where an agreement provides that no cause of action shall accrue with regard to a dispute till an award is made, such provision will be regarded as nugatory and the cause of action will accrue to a party when it would normally accrue under the ordinary law, if the above cl. were absent.

Appeals (sec. 39): An appeal lies from the following orders only and no others. An order (i) superseding arbitration, (ii) on an award in the form of a special case, (iii) modifying or correcting the award, (iv) filing or refusing to file an arbitration agreement, (v) staying or refusing to stay legal proceedings, (vi) setting aside or refusing to set aside an award. The above provisions do not cover orders passed by the Small Causes Court. Further, no second appeal lies from the above orders, though an appeal to the Supreme Court is competent (ibid).

Costs (sec. 38): If the arbitrators refuse to file the award in Court without payment of their fees and a party disputes the amount claimed by them, the party may deposit the amount claimed in Court and the Court will then order the arbitrator to file the award in Court and will thereafter, after due inquiry, order a just sum to be paid to the arbitrators, out of the moneys deposited and refund the balance to the party (ibid). The Court has also power to make such order as to the costs of the arbitration proceedings as it thinks fit when the award contains no sufficient provision regarding thereto (ibid).

(c) *Parker etc. Co. v. Turpin* (1918), 1 K.B. 358; *Adams v. Catley* (1892), 66 L.T. 687; *Jadavji v. Hirachand*, 55 Bom. L.R. 918.

(d) *Anglo-Persian Oil Co. v. Panchappa*, 45 M.L.J. 653.

CHAPTER XVIII

MORTGAGES AND CHARGES *

Mortgage defined: A mortgage is "a transfer of an interest in specified immoveable property, for the purpose of securing the payment of money advanced or to be advanced by way of loan, an existing or future debt or the performance of an engagement, which may give rise to a pecuniary liability" (sec. 58). The transferor is called the "mortgagor", the transferee the "mortgagee" and the principal money and interest of which payment is secured is called the "mortgage money". The instrument by which the transfer is effected is called the "mortgage deed".

A mortgage is thus a transfer of an interest in specified immoveable property, as security for payment of a debt. The creation of a right in property, as accessory to the right to recover a debt, is, therefore, the chief characteristic of a mortgage. It is thus distinguished from a "covenant not to alienate", which does not involve any transfer of interest in property. Similarly, it differs also from a "sale with a condition of re-transfer", in which, no relationship of debtor and creditor exists, and in which no partial rights in property are transferred but all rights are transferred with the exception of the qualified right of re-purchase. Notice that in India, "an agreement to mortgage" does not amount to an equitable mortgage as in England (e). It only creates a personal obligation, which cannot be enforced by specific performance.

Charge distinguished: Transfer of an interest in property also distinguishes a mortgage from a "charge". In a charge, no right is created as against the property which is subject to the charge, but only a right to have the debt satisfied out of that property. A mortgage, therefore, is good as against subsequent transferee with or without notice, while a "charge" is good against a subsequent transferee, only if he is such with notice of the charge or is a volunteer (f) (sec. 100). A mortgage requires to be attested by two witnesses, but a "charge" does not require such formality. A "charge" may be created by operation of law; a mortgage cannot be so created. Again, there is no personal covenant to repay in case of a "charge", in a simple mortgage, there is such a covenant. A mortgage is for a fixed term, it cannot be in perpetuity; a charge may be in perpetuity. Lastly, in a simple mortgage, a power of sale is expressly or impliedly conferred on the creditor; it is otherwise in case of a charge (sec. 100). Notice that a mortgage may be for a debt due or for an advance to be made in future.

Kinds of mortgages

(1) "Simple mortgage": "Where without delivering possession of the mortgaged property, the mortgagor binds himself personally to pay the mortgage money and agrees expressly or impliedly, that in the event of his failing to pay according to the contract, the mortgagee shall have a right to cause the mortgaged property to be sold, and the proceeds of sale applied, so far as may be necessary, in payment of the mortgage money, the transaction is called a 'simple mortgage' and the mortgagee, a 'simple mortgagee'" [sec. 58, cl. (b)]. A simple mortgage thus consists of (i) a personal covenant to repay; (ii) a transfer of a right to cause the property to be sold if the debt is not repaid and (iii) an absence of transfer of possession.

(2) "Mortgage by conditional sale": "Where the mortgagor ostensibly sells the mortgaged property, on condition that on default of payment of the mortgage money on a certain date, the sale shall become absolute or on condition that on such payment being made, the sale shall become void, or on condition that on such payment being made, the buyer shall transfer the property to the seller, the transaction is called a 'mortgage by conditional sale' and the mortgagee, a 'mortgagee by conditional sale'"

* References throughout are to the "Transfer of Property Act".

(e) *Manecklal v. Saraspur Manufacturing Co.*, 29 Bom. L.R. 253.

(f) *Kisonlal v. Gangaram*, 13 A.J. 25.

[sec. 58, cl. (c)]. Here, (i) the mortgagor ostensibly sells the property to the mortgagee on conditions, which may be (a) that in default of payment on the due date, the sale is to become absolute, or (b) that on such payment, the sale is to be void or (c) that on such payment, the property is to be transferred. Such a mortgage will not be regarded as such, unless the "conditions" are embodied in the document effecting the sale. Notice that in case of such mortgages, the "sale" does not become absolute, on failure of payment as agreed, but there always remains in the debtor, a right of redemption (sec. 60).

(3) "Usufructuary mortgage": "Where the mortgagor delivers possession or expressly or by implication binds himself to deliver possession of the mortgaged property to the mortgagee and authorises him to retain such possession until payment of the mortgage money, and to receive the rents and profits accruing from the property or any part of such rents and profits and to appropriate the same in lieu of interest or in payment of the mortgage money or partly in lieu of interest or partly in payment of mortgage money, the transaction is called a 'usufructuary mortgage' and the mortgagee, an 'usufructuary mortgagee'" [sec. 58, cl. (d)]. In such mortgages: (i) the mortgagor delivers or agrees to deliver possession of the mortgaged property to the mortgagee and (ii) authorises him to retain possession thereof till repayment of the mortgage money; (iii) to receive, in the meanwhile, the rents and profits or part thereof and (iv) to appropriate the same towards repayment of interest or principal or both. In such mortgages, the mortgagor cannot be sued personally for the debt, because the mortgagee looks to the rents and profits for repayment. "Zuripeshgi" leases must be distinguished from such mortgages. They are really loans for a premium. If however they are really intended to secure a debt, the transaction will be a mortgage, by whatever name called (g).

(4) "English mortgage": "Where the mortgagor binds himself to repay the mortgage money on a certain date, and transfers the property absolutely to the mortgagee, but subject to the proviso that he will re-transfer it to the mortgagor upon payment of the mortgage money as agreed, the transaction is called an 'English mortgage'" [sec. 58, cl. (e)]. In such mortgages, (a) there is a transfer of ownership to the mortgagee, (b) with a covenant to repay the debt on a certain day and (c) a proviso that on such condition being performed, the mortgagee shall re-transfer the property to the mortgagor. In such cases, the personal liability of the mortgagor remains, notwithstanding the conveyance. The mortgagee also becomes entitled to possession of the mortgaged property.

(5) "Mortgage by deposit of title deeds", also called "equitable mortgage": "Where a person in any of the following towns, viz. Calcutta, Madras, Bombay and in any other town, which the State Government concerned, may, by notification in the Official Gazette, specify in this behalf, delivers to a creditor or his agent, documents of title to immoveable property, with intent to create a security thereon, the transaction is called a 'mortgage by deposit of title deeds'" [sec. 58, cl. (f)]. This is a mortgage which is created by a mere deposit with the creditor of a title deed or title deeds, relating to the mortgaged property, with the intention of creating a security thereon. It does not require any writing or registration. It can be created by such deposit only in Calcutta, Madras and Bombay and in such other towns as may be notified by the State Government. All title deeds need not be deposited but the title deed deposited must show apparent title in the depositor. Intention to create a security is the essence of the transaction. Hence a deposit of title deeds with a view to prepare a legal mortgage does not amount to an equitable mortgage (h). If the deposit is accompanied by a writing which is the contract of mortgage itself, it must be registered (i). If it merely records a transaction already carried out, it need not be registered (j). The property may be situated anywhere.

(6) Anomalous mortgages: These are mortgages which do not fall within any of the above five classes, e.g. a simple mortgage, usufructuary mortgage, mortgages by condi-

(g) Bengal Indigo Co. v. Raghubar Das,
23 I.A. 158.

(h) Madras Deposit Co. v. Oonamalai, 18
Mad. 29.

(i) Vernon v. Barcell (1762), 1 Eden, 113.

(j) Varatha Pillai v. Jeevarathammal, 46
I.A. 285.

tional sale, English mortgage or equitable mortgage [sec. 58, cl. (g)]. San mortgages of Gujarat and Kanom mortgages of Madras are illustrations of such mortgages.

(7) "Sub-mortgages": This is a mortgage created by the mortgagee, on his mortgage interest, for securing a debt due by himself to the sub-mortgagee. A "sub-mortgage" requires registration. A "sub-mortgage" may be created by deposit of title deeds. (8) As regards mortgage of moveables see ante.

Mortgage: how created: Where the principal money secured is Rs. 100 or upwards, a mortgage (not being an equitable mortgage), can only be created by (i) a registered instrument (ii) signed by the mortgagor and (iii) attested by two witnesses. In other cases, it may be effected (i) as above or (ii) by delivery of possession (except in case of simple mortgages) (sec. 59). Notice that if the mortgage deed is not properly registered, it cannot operate as a mortgage. It cannot also operate as a charge. It can be admitted in evidence, however, to prove collateral facts, e.g. the character and nature of possession of the "mortgagee" or the fact of the debt. Notice further that on registration, the mortgage becomes operative from the date of execution and not that of registration.

Rights of mortgagor

(i) **Right of redemption:** This is a right to redeem the mortgage property, on payment or tender to the mortgagee of the mortgage money, after the same has become due. The right includes: (a) a right to return of all documents relating to the mortgaged property, including the mortgage deed, in possession of the mortgagee; (b) to obtain delivery of possession of the mortgaged property from the mortgagee where the latter is in possession thereof; (c) to obtain a re-transfer of the same to himself or his nominee (at his own cost) and (d) to a registered acknowledgment from the mortgagee (where the mortgage is registered), to the effect that the mortgagee's rights re: the property, are extinguished. These rights can be enforced by suit also (sec. 60). A mortgagor, having a share in the mortgage property, however, is not entitled to redeem his share, on payment of a proportionate amount, unless the mortgagee has acquired, in whole or in part, the share of the other co-mortgagor. Further, if the due date of payment expires, the mortgagee is entitled to reasonable notice before payment, if the mortgage deed so provides. Notice that the right of redemption is available to the mortgagor only if (i) it has not been extinguished by acts of parties or (ii) by a decree of the Court (*ibid*).

"**Clog on redemption**": The right of redemption, also called "the equity of redemption", is a statutory right, which cannot be fettered by any restrictions, which prevent or obstruct its exercise. Such a provision is called a "clog on redemption", and is regarded by law as void. The principle of law is "once a mortgage, always a mortgage". Thus a condition converting a mortgage into a sale, on failure to repay on the due date is bad (*jj*). There is nothing, however, to prevent the mortgagee from buying up the property subsequently. A condition postponing the right of redemption for a particular period, if repayment is not made on the due date, is also bad for the same reason (*k*). A stipulation for a penalty in case of default is regarded as a "clog" and is relieved against. Where by the terms of a mortgage, the mortgagee secures a collateral benefit for himself, it is a question of fact in each case, whether it is a "clog" or not. If the collateral benefit extends beyond the term of the mortgage, e.g. a permanent lease, it would be void (*l*). A right of pre-emption to the mortgagee, which is exercisable by him after redemption, has been held to be not a clog in England (*m*). Of course, an independent agreement entered into by the mortgagee after the mortgage, affecting the mortgaged property or the right of redemption, is not a "clog" (*n*). An agreement to sell the property to the mortgagee at a fixed rate, if the mortgage is not redeemed, has, however, been held to be a "clog" and, therefore, bad in law (*o*).

(*jj*) *Varatha Pillai v. Jeevarathammal* (supra).

(*k*) *Mahomed Sherkhan v. Sheth Swami Dayal*, 49 I.A. 60.

(*l*) *Subrao v. Manjappa*, 16 Bom. 705.

(*m*) *Krelinger v. New Patagonia Co.* (1914), A.C. 25.

(*n*) *Noakes & Co. v. Rice* (1902), A.C. 24.

(*o*) *Viranna v. Pallaya* (1947), 1 M.L.J.

Notice that a mortgage security is one and indivisible. It cannot therefore be redeemed in parts. The only case when such partial redemption is permissible is where the mortgagee has acquired a share in the mortgaged property. The owners of the remaining shares can then redeem their shares, by payment of proportionate amount. The mortgagor, on redemption, is also entitled to call upon the mortgagee to assign the mortgage debt and transfer the mortgaged property to such third person as the mortgagor may direct (sec. 60A).

(ii) **Right of inspection:** The mortgagor is entitled, at his own costs, to get inspection and copies of documents relating to the mortgaged property in the possession of the mortgagee, so long as the right of redemption subsists (sec. 60B).

(iii) **Right to redeem separately:** A mortgagor who has executed two or more mortgages (on the same or different properties), is entitled to redeem any one of them, without being compelled to redeem them all unless the contract otherwise provides (sec. 61). In other words, *consolidation of mortgages* against the mortgagor is not allowed by law, unless the contract otherwise provides.

(iv) **Right to possession:** In case of usufructuary mortgage, the mortgagor is entitled to recover possession of the mortgaged property from the mortgagee on the mortgage debt being repaid in part or in whole from the usufruct and on the payment of the balance (if any) (sec. 62).

(v) **Right to "accessions":** Where the mortgaged property receives any accession during the continuance of the mortgage, the mortgagor shall, on redemption, in absence of a contract to the contrary, be entitled to the same, provided that (a) if the accession can be separated, he shall pay the expenses of acquiring the same to the mortgagee. (b) If it cannot be separated, he shall pay the cost thereof to the mortgagee, only if such accession was necessary to preserve the property from destruction, forfeiture or sale or if it was made with the assent of the mortgagor. Interest at the mortgage rate or at 9 p.c. if no rate is fixed shall be payable on such cost (sec. 63).

Accessions may be natural or acquired. Instances of the latter are new trees, a new well, adding a new storey. Notice that as regards "accessions" which cannot be separated, they must, on redemption, be handed over to the mortgagor, who is not bound to pay compensation for the same to the mortgagee, unless the case comes within the words of the sec.

(vi) **Renewal of lease:** If the mortgagee of a leasehold obtains a renewal thereof during the continuance of the mortgage, the mortgagor is entitled to the benefit of the new lease, on redemption, unless the contract otherwise provides (sec. 64).

(vii) **Improvements:** Where the mortgaged property is improved by the mortgagee during his possession thereof, the mortgagor on redemption is, in absence of a contract to the contrary, entitled to such improvements. The mortgagor is bound to pay the cost thereof to the mortgagee, only if (a) they were necessary to preserve the property from destruction or deterioration or to prevent the security being insufficient or (b) if they were made under the lawful orders of any public servant or authority. Interest at the mortgage rate or at 9 p.c., if no rate is fixed, is also payable thereon. Profits resulting from such improvements must be credited to the mortgagor (sec. 63A).

Generally the mortgagee cannot be allowed "to improve the mortgagor out of the estate". He is allowed reasonable costs of improvements, only if his case falls within any of the above two cls. Thus rebuilding the mortgaged property at a cost exceeding five times the mortgage amount will not be justified.

(viii) **Deposit in Court:** The mortgagor can, after the date for redemption has passed, deposit the mortgage amount due according to him, in Court. On such deposit being made, the Court will serve a written notice thereof on the mortgagee. If the mortgagee accepts the payment, he can withdraw the moneys deposited in Court, on his depositing in Court the mortgage deed and all other documents relating to the mortgaged property in his possession, which shall then be handed over to the mortgagor. If the mortgagee has been in possession of the mortgaged property, he can also be called upon to deliver possession to the mortgagor and (at mortgagor's costs), to execute

a re-transfer of the property to the mortgagor or his nominee (sec. 83). If the amount is found to be the proper amount due, the mortgagee shall not be entitled to any interest after the date of the deposit (sec. 84).

Implied covenants by the mortgagor: A mortgagor is impliedly deemed to have contracted that (a) the interest he professes to transfer subsists and that he has power to transfer it; (b) that he will defend or enable the mortgagee in possession to defend the mortgagor's title thereto; (c) that he will pay all public charges accruing in respect of the mortgage property while in his possession; (d) if the mortgage property is a lease, that he will perform all the conditions and covenants thereof and pay the rent payable in respect thereof, so long as the mortgage subsists, and that he has done so till the date of the mortgage; (e) that he will pay off all interest due and the principal amounts of all prior incumbrances, on the due dates (sec. 65). The benefits of these covenants can be claimed by all persons claiming under the mortgage.

Power to give lease: The mortgagor's power to grant leases of the mortgage property, while in his possession, must be exercised by him, only as follows: (a) the lease must be such as would be made in ordinary course of management of the property; (b) best rent shall be reserved; (c) no premium shall be payable, and no rent in advance can be taken; (d) no covenant for renewal shall be made. (e) The lease must take effect not later than 6 months of the date thereof. (f) A lease of buildings shall not be for more than 3 years and shall contain a covenant for re-entry, if rent is not paid on the fixed date. These rules can be modified, however, by mutual consent. Similarly, the power to grant leases may also be excluded by contract (sec. 65A).

Waste: A mortgagor in possession, is not liable for deterioration of the property; but he must not commit waste, which (a) is destructive or (b) permanently injurious thereto or (c) which makes the security insufficient. Instances of waste are felling timber, removing fixtures, pulling down buildings, etc. (sec. 66).

Rights of mortgagee

The mortgagee has the following rights, after the mortgage debt has become due: (1) to file a suit for *foreclosure* or *sale* of the mortgage property (sec. 67). A suit to obtain a decree that the mortgagor shall be absolutely debarred of his right to redeem the mortgaged property, is called a "suit for foreclosure". Notice however that a simple mortgagee cannot foreclose. His right is to sue for sale. Limitation for a suit for sale is 12 years from the time the mortgage money becomes due (art. 132). A usufructuary mortgagee cannot sue either for sale or for foreclosure. This is because it is on those terms that the mortgage is created. He can only remain in possession till the mortgage money is paid off. A mortgagee by conditional sale can only sue for foreclosure. This is because the property is already sold to him under the mortgage. On the other hand, an English mortgagee can only sue for sale. He cannot foreclose. The remedy of an equitable mortgagee also is a suit for sale, as provided by sec. 67. Notice that the mortgagee of a railway, canal or other public work is prohibited by the sec. from suing for sale as well as foreclosure. Notice further that the mortgage security being one and indivisible, there can be no partial foreclosure or sale [sec. 67, cl. (d)]. Thus one of several mortgagees cannot sue for foreclosure or sale in respect of his fractional share of the mortgage security. This is allowed only where the mortgagees have severed their interests under the mortgage with the consent of the mortgagor. Similarly, where the mortgagee holds different mortgages of different properties of the same mortgagor, or successive mortgages on the same property of the mortgagor, he is bound in law, to enforce in one suit, all his mortgages against the same mortgagor and not split up his mortgages into different suits, unless the contract otherwise provides (sec. 67A). In other words, "*consolidation*" is compulsory against the mortgagee, though it is not compulsory in case of the mortgagor (see sec. 60).

(2) A mortgagee may also *sue for the mortgage money*. This right is available to him only if (i) the mortgage deed contains a covenant to repay; (ii) where, without any fault of the mortgagor or the mortgagee, the mortgaged property is wholly or partially destroyed and the mortgagor fails to make up the amount of the security, though called upon by the mortgagee to do so; (iii) where the mortgagee is deprived

partly or wholly of his security by the wrongful act or default of the mortgagor; (iv) where the mortgagee being entitled to possession of the mortgaged property, the mortgagor fails to secure the same to the mortgagee (sec. 68). In cases (i) and (ii), the Court may stay the suit and require the mortgagee to enforce his claim first, against the mortgage security. A transferee from the mortgagor, or his legal representatives, cannot also be sued on the personal covenant (*ibid*).

(3) The mortgagee has also a right to *sell the mortgaged property without the intervention of the Court*. The power is exercisable only (a) where the mortgage is an English mortgage and none of the parties is a Hindu, Mahomedan or Buddhist, or any of the notified classes, or (b) where the mortgagee is the Crown and such power is expressly given by the mortgage deed, or (c) where the mortgaged property is situate in any of the Presidency Towns and such power is expressly given by the mortgage. The power, however, cannot be exercised, unless (a) written notice for payment of the principal amount is served on the mortgagor and a default has occurred for 3 months or (b) unless interest, not less than Rs. 500, is unpaid for 3 months after it is due (sec. 69).

(4) The mortgagor can also *appoint a receiver of the income of the mortgaged property* (under sec. 69A), in cases where he has power of sale under sec. 69. If a person is named in the mortgage deed, he can be appointed such receiver. If no such person is mentioned, the mortgagee may appoint as receiver a person agreed to by the mortgagor. Failing such agreement, the mortgagee must apply to the Court to make a suitable appointment. Such receiver is regarded as the agent of the mortgagor. He is entitled to recover the income of the mortgaged property, to give valid receipts and file suits for making such recoveries. Out of moneys so recovered, he is bound to discharge all rates, taxes, etc. accruing due with regard to the mortgaged property, all annual sums, which have priority over the mortgage in question, premiums due or payable under the mortgage or under the Act and costs of such repairs as are desired by the mortgagee in writing. The balance must be used in payment of the interest due and the principal.

(5) The mortgagee is also entitled to the *benefit of any accession to the mortgaged property*, while the mortgage continues (sec. 70), e.g. digging a well or setting up an electric installation on the mortgaged property by the mortgagor. It does not matter whether the mortgagee is in possession or not.

(6) If the mortgagor obtains a *renewal of a lease*, the mortgagee is similarly entitled to the benefit thereof during the continuance of the mortgage (sec. 71).

(7) If the mortgaged property is *sold for arrears of land revenue* or is acquired under the Land Acquisition Act or otherwise, the mortgagee is entitled to claim payment of the mortgage amount or part thereof, out of the proceeds of such sale or acquisition (sec. 73).

Rights of mortgagee in possession (sec. 72): A mortgagee in possession is entitled, out of recoveries made by him, to spend moneys for the following: (a) for the preservation of the mortgaged property from forfeiture, destruction or sale; (b) for supporting the mortgagor's title to the property; (c) for making his own title good against the mortgagor; (d) for renewal of lease, if the mortgage is of a leasehold. Sums spent as above may be added to the principal sum due under the mortgage and shall carry interest at the mortgage rate. (e) The mortgagee can also insure the property, if the mortgagor has not done so, but not for more than two-thirds of its value. Premiums paid under such policy can be added to the principal amount and shall carry the same rate of interest.

Liabilities of mortgagee in possession (sec. 76)

He must (i) manage the property as a man of ordinary prudence; (ii) must use his best endeavours to collect the rents and profits; (iii) out of the income, pay all revenue and other public charges and rent (if any) payable; (iv) must make such necessary repairs, as he can pay for out of balance of rents and profits, after deducting payments under (iii) and interest; (v) he must not be guilty of any act which is

destructive or permanently injurious to the property; (vi) he must apply insurance moneys, if received, in re-instating the property; (vii) must keep clear, full and accurate accounts of income and expenditure, supported by vouchers and supply true copies thereof to the mortgagor at his request and cost; (viii) after deducting from receipts, costs of management and collection charges and items (iii) and (iv), apply the balance in reduction of interest and/or principal. (ix) If and when the mortgagor pays or tenders the mortgage amount, he shall account for gross receipts, without any deductions, from the date of such payment or tender. If the mortgagee fails in these duties, he is liable to the mortgagor in damages.

Priority (sec. 78): Mortgages rank in order of execution. If however (i) through the fraud, misrepresentation or gross neglect of a prior mortgagee, a subsequent mortgagee is induced to advance moneys on the security of the mortgaged property, the prior mortgagee shall rank after the subsequent mortgagee; (ii) if a mortgage is made to secure future advances upto a maximum, a subsequent mortgagee, with notice of the prior mortgage, will be postponed, as regards such later advances, upto the maximum (sec. 79).

No mortgagee, paying off a prior mortgage, will thereby acquire priority with regard to his mortgage, except as above (sec. 93). Thus no "tacking" is allowed by law to a mortgagee.

Marshalling (sec. 81): Where two or more properties are mortgaged to one mortgagee and thereafter one or more of these, are mortgaged to another person, the latter mortgagee in absence of a contract to the contrary, is entitled to call upon the former mortgagee to satisfy his claim against the property not included in his own mortgage, so far as it may extend and claim the balance alone, from such latter property. This is called "marshalling of securities".

The right is however subject to certain conditions: (i) there must be a common debtor. "Marshalling" applies only where there are different debts realisable out of different properties of the same debtor. (ii) The right will not be enforced to the prejudice of the prior creditor or incumbrancer. (iii) The right may also be excluded by a contract to the contrary.

Contribution (sec. 82): (i) Where the mortgaged property belongs to two or more persons, each having a distinct interest therein, the different shares of each of the co-mortgagors in such a case, are, in absence of a contract to the contrary, liable to contribute rateably to the discharge of the mortgage debt. (ii) Where, of two properties belonging to the same owner, one is mortgaged to secure one debt and thereafter, both are mortgaged to secure another debt and the former debt is paid out of the former property, then, in absence of a contract to the contrary, each property is liable to contribute rateably to the discharge of the latter debt, after deducting the value of the former debt from the former property. This is called "contribution amongst co-mortgagors". It is the reverse of "marshalling" which operates amongst competing mortgagees.

Notice that the obligation to contribute extends only to the properties concerned, and not to the mortgagors personally. Further, it cannot and does not affect the rights of the mortgagees, against the properties mortgaged, being applicable only to mortgagors *inter se*. Lastly, the liability to contribute may be modified by the terms of the mortgage.

Who can redeem

Besides the mortgagor, (i) any person interested in the mortgage security or equity of redemption, (ii) any surety for the debt or part thereof, and (iii) any creditor of the mortgagor, who in an administration suit against him, has obtained a decree for sale of the property (sec. 91), can redeem. The above persons and a co-mortgagor, on such redemption, acquire all rights of sale and foreclosure as the mortgagee redeemed had against the mortgagor. This is called "subrogation". "Subrogation" means substitution. In it, the person who redeems is substituted for the incumbrancer who is paid off.

"Subrogation" may be of two kinds. It may be either (i) contractual or (ii) legal. Where there is an agreement that the person advancing money to pay off a mortgage,

shall be subrogated to the rights of the mortgagee who is paid off, the subrogation is "contractual" or "conventional". Sec. 92 requires, however, that the agreement in such cases should always be in writing and registered.

"Legal subrogation" means subrogation by operation of law. It arises in four ways: (i) where a puisne (i.e. intermediate) mortgagee redeems a prior mortgage; (ii) where a co-mortgagor redeems the whole mortgage; (iii) where the mortgagor's surety redeems the mortgage; (iv) where the purchaser of the equity of redemption redeems the mortgage. Notice that the mortgagor is not entitled to subrogation on redeeming a prior mortgage, because he is merely discharging his duty in so redeeming, unless of course, the subsequent mortgage was expressly made subject to the first. Similarly, "subrogation" may be excluded where there is an agreement to that effect. Notice further that there can be no partial subrogation. The prior incumbrance must be completely discharged. An equitable charge also may arise by operation of law, e.g. where a mortgagee discharges a claim against the mortgage security, e.g. revenue charges, in order to save his security from jeopardy. Where one of several co-mortgagors redeems the mortgage, he is entitled to add his costs of redemption to the mortgage debt (sec. 95).

Remedies of charge holders (sec. 100): The holder of a charge is entitled to all the remedies which a simple mortgagee is entitled to under the Act, i.e. he can sue for sale, just as a simple mortgagee can. He has no right of foreclosure. Limitation for enforcement of a charge is 12 years from the time the money is due (art. 132). The doctrine of subrogation applies to charge holders also, as also the rule as regards marshalling and contribution. The principle of consolidation of securities (sec. 65A) however has been held not to apply to charge holders. Notice that a charge cannot be enforced against a person to whom the property has been transferred for consideration and without notice of the charge.

Merger (sec. 101): Where a mortgagee of or charge holder on any immoveable property or a transferee from such persons, purchases or acquires rights in the property mortgaged or charged, e.g. by purchasing the equity of redemption, the mortgage or charge is not thereby "merged" as between himself and a subsequent mortgagee or charge holder and such latter persons are entitled to foreclose or sell the property under their mortgage or charge, only after redeeming the prior mortgage or charge or subject thereto (sec. 101). In other words, there is no extinguishment of the mortgage security by "merger", because the mortgagee or charge holder acquires the equity of redemption also. This is a simple rule, now substituted by the amended Transfer of Property Act, in place of the old rule, under which intention of the parties was regarded as the sole test.

CHAPTER XIX

REGISTRATION

Registration Act (1908): The Act lays down rules for compulsory registration of certain documents and for the consequences which result from their non-registration. The object of registering a document is (i) to give notice to the world that such a document has been executed; (ii) to prevent fraud and forgery and (iii) to secure that every person dealing with the property, transactions with regard to which require registration, has complete notice of all transactions affecting the title to the property. The Act extends to the whole of India, except such districts as are specially excluded.

Documents compulsorily registrable

These documents are described by sec. 17. These documents are compulsorily registrable, if the property to which they relate is situate in a district in which, and if they have been executed on or after the date on which Act No. XVI of 1864 or the Indian Registration Acts of 1866, 1871, or 1877, or of 1908 came or comes into force.

They are (a) instruments of gift of immoveable property ;

(b) other non-testamentary instruments which purport or operate to create, declare, assign, limit or extinguish, whether in present or in future, any right, title or interest, whether vested or contingent, of the value of one hundred rupees and upward, to or in immoveable property ;

(c) non-testamentary instruments which acknowledge the receipt or payment of any consideration on account of the creation, declaration, assignment, limitation or extinction of any such right, title, or interest ;

(d) leases of immoveable property from year to year, or for any term exceeding one year, or reserving a yearly rent. [Provided that the Provincial Government may, by order published in the Official Gazette, exempt from the operation of this sub-section any leases executed in any district or part of a district, the terms granted by which do not exceed five years, and the annual rents reserved by which do not exceed fifty rupees];

(e) non-testamentary instruments transferring or assigning any decree or order of a Court or any award when such decree or order or award purports or operates to create, declare, assign, limit or extinguish, whether in present or in future, any right, title or interest whether vested or contingent, of the value of one hundred rupees and upwards, to or in immoveable property ; and

(f) authority to adopt a son, executed after January 1872 and not conferred by will.

Certain documents, however, are excluded from (b) and (c) above. They are :

(i) any composition-deed ; or

(ii) any instrument relating to shares in a Joint Stock Company, notwithstanding that the assets of such company consist, in whole or in part, of immoveable property ; or

(iii) any debenture issued by any such company, and not creating, declaring, assigning, limiting, or extinguishing any right, title or interest to or in immoveable property except in so far as it entitles the holder to the security afforded by a registered instrument, whereby the company has mortgaged, conveyed, or otherwise transferred the whole or part of its immoveable property or any interest therein to trustees upon trust for the benefit of the holders of such debentures ; or

(iv) any endorsement upon, or transfer of, any debenture issued by any such company ; or

(v) any document not itself creating, declaring, assigning, limiting, or extinguishing any right, title, or interest of the value of one hundred rupees and upwards to or in immoveable property, but merely creating a right to obtain another document which will, when executed, create, declare, assign, limit or extinguish any such right, title or interest ; or

(vi) any decree or order of a Court, except a decree or order expressed to be made on a compromise and comprising immoveable property other than that which is the subject-matter of the suit or proceeding ; or

(vii) any grant of immoveable property by the Crown ; or

(viii) any instrument of partition made by a Revenue-officer ; or

(ix) any order granting a loan or instrument of collateral security granted under the Land Improvement Act, 1871, or the Land Improvement Loans Act, 1883 ; or

(x) any order granting a loan under the Agriculturists' Loans Act, 1884, or instrument for securing the repayment of a loan made under that Act ; or

(xa) any order made under the Charitable Endowments Act, 1890, vesting any property in a Treasurer of Charitable Endowments or divesting any such Treasurer of any property ; or

(xi) any endorsement on a mortgage-deed acknowledging the payment of the whole or any part of the mortgage-money and any other receipt for payment of money due under a mortgage when the receipt does not purport to extinguish the mortgage ; or

(xii) any certificate of sale granted to the purchaser of any property sold by public auction by a Civil or Revenue Officer.

Notice that a document purporting or operating to effect a contract for sale of immoveable property shall not be deemed to require or ever to have required registration by reason only of the fact that such document contains a recital of the payment of any earnest money or of the whole or any part of the purchase money.

Documents optionally registrable (sec. 18)

These are: (a) instruments (other than instruments of gift and wills) which purport or operate to create, declare, assign, limit, or extinguish, whether in present or in future, any right, title, or interest, whether vested or contingent, of a value less than one hundred rupees, to or in immoveable property;

(b) instruments acknowledging the receipt or payment of any consideration on account of the creation, declaration, assignment, limitation, or extinction of any such right, title or interest;

(c) leases of immoveable property for any term not exceeding one year, and leases exempted under section 17;

(cc) instruments transferring or assigning any decree or order of a Court or any award when such decree or order or award purports or operates to create, declare, assign, limit or extinguish, whether in present or in future any right, title or interest, whether vested or contingent, of a value less than one hundred rupees, to or in immoveable property;

(d) instruments (other than wills) which create, extinguish, declare, assign or limit any right, title or interest in moveable property;

(e) wills;

(ee) notices of pending suits under sec. 52 of the T.P. Act; and

(f) all documents not required by sec. 17 to be registered.

Even in these cases, however, the effect of the Transfer of Property Act is to make such documents if unregistered, invalid in law, e.g. a mortgage deed of property of less than Rs. 100 in value, leases of less than one year and deeds of gift of property, less than Rs. 100 in value. In these cases, the transaction, in order to be valid, must be completed by delivery of possession following an oral agreement or by a registered deed.

Effect of above provisions

Notice that under cl. (b) of sec. 17, instruments which themselves do not create, assign, etc. an interest in immoveable property of over Rs. 100 in value but which acknowledge or declare or record the creation, assignment, etc. of such a right in the past do not require registration (p). Similarly, an agreement to transfer, assign, etc. such property does not require registration. A writing recording the fact of an equitable mortgage also does not require registration (q). A release or surrender of right to immoveable property must be registered (r). Under cl. (c) of sec. 17, a mere receipt does not require registration except where it acknowledges receipt of a consideration for the creation, etc. of a right to immoveable property. Under cl. (d) leases for less than a year are not compulsorily registrable. Under the definition of "lease" in sec. 2(7) a "lease" includes an "agreement to lease". An "agreement to lease" however is compulsorily registrable only when it operates as a present demise (s). Under sec. 18, a sale or mortgage of moveables, a will and documents creating, transferring, etc. a right in immoveable property of less than Rs. 100 in value do not require registration.

Person entitled to register: Only the executent or a person claiming under him, or a representative or assign of such person or a person holding, from such persons, a power of attorney as provided by the Act, can present a document for registration (sec. 32).

(p) Bageshwari v. Jaggannath, 59 I.A. 130.
(q) Obla Sunderachariar v. Narayamma, 58 I.A. 68.

(r) Bhagwandas v. Mansukhlal, 33 Bom. L.R. 802.

(s) Hemant Kumari v. Midnapore Zamin-dari, 46 I.A. 240.

Time from which registration effective: A registered document operates from the date of its execution and not from the date of its registration (sec. 47).

Priority

A registered document whether relating to moveable or immoveable property is always effective against an oral agreement relating to the same property unless in the latter case possession of the property has been given to the transferee and such delivery constitutes a valid transfer in law (sec. 48). Thus an oral mortgage is postponed to a registered mortgage of the same property. A prior mortgage by deposit of title deeds however prevails over a subsequent registered mortgage of the same property (sec. 48, proviso).

Similarly, every document falling under clauses (a) to (d) of sec. 17 and clauses (a) and (b) of sec. 18, if registered, shall be effective as regards the property comprised therein against every unregistered document relating to the same property (sec. 50).

Effect of non-registration (sec. 49)

A registered document operates from the date of its execution and not from the date of the registration (sec. 47). If a document is not registered as required (i) it cannot affect property comprised therein and (ii) it cannot confer a power to adopt. (iii) It cannot be received as evidence of any transaction affecting such property (sec. 49).

Notice however that as the proviso to sec. 49 provides, an unregistered document which is compulsorily registrable can be received in evidence in a suit for specific performance of a contract represented by such document, as an evidence of part performance and also as evidence of any collateral transaction not required to be affected by a registered document.

Under the above provisions therefore an unregistered mortgage of immoveable property, an unregistered deed of sale, or an unregistered lease or deed of partition cannot be admitted in evidence for proving a mortgage, sale, lease or partition or the terms of any of the above transactions.

Such documents are admissible to prove (a) the nature of possession, (b) as evidence of a relationship, (c) as evidence of an acknowledgment of a debt and for any other collateral purpose. They can also be used in suits for specific performance of a contract to sell, lease or mortgage the property referred to in the documents as provided by sec. 53A of the Transfer of Property Act.

Notice that a registered document prevails over an oral agreement unless the latter is followed by delivery of possession and amounts to a valid transfer in law (sec. 3, Transfer of Property Act). Similarly, a registered document prevails over an unregistered document, when registration is compulsory (sec. 50).

Time for presentation: All documents requiring registration must be presented to the proper officer for registration within four months from the date of their execution (sec. 23). Exception is made in case of wills which can be registered at any time. Where a document is not presented for registration as above through unavoidable accident, it can be presented for registration thereafter, provided the delay does not exceed four months and a fine not exceeding 10 times the registration fee is paid (sec. 25). Documents executed outside India must be presented for registration within four months of their arrival in India (sec. 26).

Place of registration: All documents compulsorily registrable under sec. 17, sub-sec. (1), cls. (a), (b), (c) and (d) and sec. 18, cls. (a), (c), (cc), and (ee) must be presented for registration in the office of the Sub-Registrar within whose district the whole or some portion of the property to which the documents relate is situate (sec. 28). All other documents may be registered either where they are executed or at any other Sub-Registry as the persons executing the same desire (sec. 29).

CHAPTER XX

LIMITATION

Limitation : Meaning : The Limitation Act of 1908 deals with the law of limitation and prescription. "Limitation" means, the period of time prescribed by law after which a suit or proceeding with regard to a particular violation of a legal right, is not maintainable in a Court of Law. "Prescription" means the period of time, prescribed by law, on the determination of which, a substantive right is acquired or extinguished. The law of limitation is based on the maxim "*vigilantibus et non dormientibus lex succurrit*" which means that the law helps the diligent. Limitation bars the remedy but not the right; "prescription" extinguishes a right.

The Act : The Act is divided into two parts. The first portion deals with general rules for computing the period of limitation, under various circumstances. The second portion, i.e. the schedule, gives specific periods of time for specific causes of action with regard to specific cases.

General Rules as to application of limitation : The first part of the Act lays down certain rules as to how the provisions of the Act are to be applied when a question of limitation arises. These rules are :

(1) Every suit, appeal or application filed after the expiry of the period prescribed for limitation must be dismissed, whether the point of limitation has been taken as a defence or not (sec. 3). The Limitation Act often works as a hardship but the Courts have no option in the matter. However hard a case may be, the rules of limitation must be strictly applied, with all the necessary consequences.

Courts closed : (2) Where the period of limitation expires on a day when the Courts are closed, the suit, appeal or application must be filed on the day the Court reopens (sec. 4).

Time extended : (3) In the following cases only, is an extension of time permissible. In case of an appeal or application for review or leave to appeal (and such other applications to which this provision is made applicable), if the appellant or applicant satisfies the Court that he had "sufficient cause" for not filing the appeal or application in time, the Court may admit the appeal or application after the limitation period has expired (sec. 5).

Notice that the sec. has no application to suits. They must always be filed in time. "Sufficient cause" does not cover negligence of a party. Being misled by an order, judgment or practice of the Court however, would be a "sufficient cause". Mistaken advice given by a pleader or other legal adviser has been held to be "sufficient cause", *Rajendra Bahadur v. Rajeshwar Bali*, A.I.R. (1937), P.C. 276, provided it is *bona fide* and proper action has been taken within a reasonable time after discovery of the mistake *Gopal Chandra v. Soloman*, 13 Cal. 62. Illness may also be sufficient cause *Girdhari v. Bhupal Singh*, A.I.R. (1923) All. 516.

Legal disability—effect of

(i) Where the person entitled to file a suit or make an application for execution is a minor or a lunatic at the time from which the period of limitation is to be reckoned, he may institute such suit or make such application, within the prescribed period of limitation, after the disability has ceased, as he would have been otherwise entitled to, if he was not suffering from the disability (sec. 6).

(ii) If he is suffering from two such disabilities, the prescribed period of limitation would begin to run after both the disabilities have ceased.

(iii) If the disability continues till his death, his legal representatives would be similarly entitled to the benefit of the same prescribed period. If the legal representative is also under a similar disability the same rules will apply in his case also (*ibid*).

(iv) Where, of several persons jointly entitled to file a suit or make an application for execution, one or more of them is or are under disability, time would not run against them, till such disability has ceased, if the concurrence of all is necessary in order to give a valid discharge; otherwise, if a valid discharge can be given without the concurrence of the person or persons under disability (*ibid*).

(v) The above rules do not apply to suits to enforce right of pre-emption (sec. 8).

(vi) *In no case, extension of time as envisaged by the above rules, will be allowed for more than 3 years, after the disability has ceased* (sec. 8).

(vii) Notice further that once time of limitation has begun to run, a subsequent disability will not stop its running (sec. 9), except where a debtor obtains Letters of Administration to the estate of the creditor, in which case, limitation will not run against the creditor till administration has ceased.

The above rules lay down the effect which the legal disability of minority or insanity of the person entitled to sue has on the period of limitation.

A minor or insane person, being by law incapable of filing an action for himself, the law in its beneficence, rules that the period of his minority or insanity, shall be excluded in calculating the period of limitation against him. If a person is suffering from both the infirmities, the whole period during which they subsist is to be excluded. It is immaterial in this connection that the minor has a guardian or that the lunatic has a committee to look after his affairs. Even in such cases, the prescribed period of limitation will begin to run only after the disability has ceased.

The above principle, however, is subject to two conditions: (i) If once limitation has begun to run, a supervening disability will not stop its running. (ii) In no case can the period of limitation be extended beyond three years of the disability ceasing. The two above conditions may be illustrated as follows:—

Where adverse possession has started against the owner of an immoveable property, his death, leaving a minor son, will not have the effect of suspending limitation during the minority of the son. Nor can the son take advantage of rules (i), (ii) and (vi) above and claim a right to file a suit to remove his adversary from wrongful possession, within 3 years of his minority ceasing. The principle of the rule is that where a cause of action has arisen, limitation will start to run at once and if it has started once, a subsequent disability will not stop its running.

The second condition may be illustrated as follows: A is entitled to a legacy under a will for recovering which the prescribed period of limitation is 12 years. At the time when the legacy is payable, i.e. at the time of the death of the deceased, A is a minor. He therefore cannot file a suit to recover the legacy. Supposing he attains majority, 11 years after the testator's death, he should have, under rule (i) above, a further period of 12 years after attaining majority to file such suit. But rule (vi) above overrides rule (i). Hence, A will have only 3 years after attaining majority within which to file such suit.

The ratio of rule (i) therefore is that it is *only* if the person concerned was under disability *at the time when the cause of action arose*, that law gives him extension of time for filing suit, for proper relief, after the disability has ceased. If, however, there was a person in existence at the time when the cause of action arose, who could lawfully file a suit for redressing the wrong, the limitation will not stop running but the right to sue will be barred at the end of the prescribed period, notwithstanding that, during the intervening period, the actual claimant was a minor or a lunatic.

Notice that no disability other than minority and lunacy is protected. Further, the secs. do not apply to appeals. What is the starting point of limitation in a given case may be a matter of debate in certain circumstances. Notice that legal representatives of a person who dies after the disability has ceased, will not get the benefit of rule (iii) above. As to rule (iv), the case of a debt due to a partnership may be considered. If out of two partners, one is a minor, but the other has authority to discharge a partnership debt, time would run against the partnership from the date when the debt became due. It would be otherwise, when the major partner has no authority to discharge the debt, without the concurrence of the other.

Suits against trustees

(i) Under sec. 10 of the Act no suit against a person "in whom property has been vested for any specific purpose" or against his legal representatives for (a) following trust property or (b) for the proceeds thereof or (c) for account of such property or proceeds, is barred by *any length of time*.

(ii) Property belonging to a Hindu, Mahomedan or Buddhist religious or charitable endowment, is regarded for this purpose as property vested in their managers "for a specific purpose" and such managers are to be regarded as trustees thereof.

(iii) The above provisions have no application to assigns for valuable consideration from such managers and trustees.

The object of the above rules is to provide that *as against an Express Trustee* there shall be no bar of limitation as regards suits for (i) recovery of trust property, (ii) or the proceeds thereof, if alienated by the trustee wrongfully or (iii) for accounts thereof.

Notice that the sec. only refers to "express trustees", i.e. persons who hold property, the beneficial interest in which is expressly vested in another person. A person in a fiduciary position to another, e.g. a partner, agent, executor or director of a company is not necessarily an express trustee. A person who intermeddles with the property of a deceased person, e.g. a *trustee de son tort*, is also not covered. As regards these persons the normal period of limitation would apply. Shebait of temples and Mahants of Maths, however, are now within the sec. Notice that limitation is not applicable only to certain class of suits against express trustees. Thus a suit against an express trustee for damages or for conversion is not covered by the sec.

Foreign contracts and limitation: Suits filed in Indian Courts on foreign contracts are governed by the provisions of the Indian Limitation Act on questions of limitation.

Where however foreign law of limitation has the effect of extinguishing all liability under a contract, such rule of foreign law can be pleaded in defence in a suit on the contract in Indian Courts provided the parties were domiciled in such foreign country for the period required by such foreign law (sec. 11).

Period of limitation—how computed

Secs. 12-25 lay down certain rules according to which the period of limitation is to be calculated in a given case. These rules are noticed below:—

(i) In case of every suit, appeal and application, the day from which limitation is to begin should be excluded (sec. 12). (ii) In case of an appeal, application for leave to appeal and application for review, the day on which judgment was pronounced and time occupied in obtaining a copy of the decree or order in question, should be excluded (*ibid*). (iii) Where a decree is appealed from or sought to be reviewed, time occupied in obtaining copy of the judgment on which the decree is based should be excluded (*ibid*). (iv) Where an award is sought to be set aside, time taken in obtaining copy of the award should be excluded (*ibid*).

Absence from India

(v) In computing period of limitation, the time during which the defendant was out of India or out of territories, beyond India, administered by the Central Government should be excluded (sec. 13). Notice that under the sec. the periods need not be continuous or contiguous. The whole period has to be excluded. Ignorance of the plaintiff that defendant is within India, will not prevent time from running.

Proceedings in Court without jurisdiction

(vi) In computing the period of limitation, the time during which the plaintiff was (1) prosecuting (2) with due diligence (3) in good faith (3) another civil proceeding against the defendant (5) founded on the same cause of action shall be excluded if (6) the suit or proceeding has failed from defect of jurisdiction or other cause of a like nature (sec. 14). The sec. gives relief where the plaintiff has filed his suit first in a

wrong Court which therefore dismisses the suit. In such a case, if a second suit is filed by the plaintiff on the same cause of action against the same defendant in a proper Court, the time taken up by the infructuous first suit will be excluded in computing the period of limitation.

For this rule to apply, however, it is necessary that (1) the first suit should have been filed *bona fide*, (2) it must have been prosecuted with due diligence, and (3) it should have been dismissed on ground of want of jurisdiction or other like cause; in other words, not on merits, after a full trial. Lastly (4) the second suit must be against the same defendant and on the same cause of action. Thus where leave of Court is necessary to file a suit against the defendant, and such leave not being taken, the first suit is dismissed, and a second suit is thereafter filed against the defendant on the same cause of action with leave, the time taken up by the first suit will be excluded in computing limitation; similarly, in case of a suit filed by a partnership without previous registration; also in case of misjoinder or non-joinder of parties, etc. Notice that the date of filing the first suit and the date of its dismissal will also be excluded (*ibid*).

Suspension of proceedings: (vii) Similarly, where the filing of a suit or application for execution is stayed by an injunction or order of Court, the time during which the injunction or order continues, the day on which the order is made and the day on which it is dissolved are to be excluded (sec. 15).

(viii) Where law requires notice to be given before filing a suit (e.g. under sec. 80 of the Civil Pro. Code in case of suit against Government), the period of notice should be excluded (*ibid*).

(ix) In suit for possession by purchaser at Court sale, the time taken up in proceeding to set aside the sale should be excluded (sec. 16).

Effect of death

(x) Where a person who would have a right of filing a suit or making an application, if living, dies before such right accrues, limitation would run against his estate only from the time there is a legal representative capable of filing a suit or application on behalf of his estate, e.g. where a debt is due to the deceased which becomes payable after his death, limitation will not run against his estate until there is some legal representative of his estate, e.g. administrator or executor or heir, who can file a suit on behalf of his estate. The same rule applies where the defendant, e.g. the debtor dies before the right of filing a suit or making an application accrues. In such a case, limitation would not run in his favour till there is a legal representative of his estate, against whom such a suit can be filed (sec. 17). These rules however do not apply to suits for pre-emption, for possession of immoveable property and for a hereditary office (*ibid*).

Effect of fraud

(xi) Where by means of fraud, a person entitled to file a suit or make an application, is kept in ignorance of his right, or where by fraud, any document on which his right is based (e.g. a will) is concealed from him, limitation shall be computed from the time when such person came to know of the fraud or was capable of having the concealed document produced. Of course, this rule applies only when the suit is filed against the person guilty of the fraud or any person claiming through him, other than a transferee in good faith and for valuable consideration (sec. 18).

Effect of acknowledgment

Under sec. 19 of the Act, if before the expiry of the period of limitation for any suit or application with regard to any right or property, an acknowledgment of liability (i) in writing (ii) signed by the person liable or by a person through whom the latter claims, is made (iii) to the claimant or (iv) any other person, a fresh period of limitation will begin from the date of such acknowledgment.

An acknowledgment of liability is sufficient, even if it is accompanied by a refusal to pay, or by a claim for set-off or by a statement that the time for payment has not arrived. It is not bad because it does not specify the exact nature of the right or

property. If the acknowledgment does not bear a date, oral evidence of date can be given, but oral evidence cannot be given of its contents.

The signature on the acknowledgment may be of the party liable or of an agent of such party duly authorised in that behalf. In case of minors and lunatics, their lawful guardians and managers are such agents (sec. 21). Similarly, in case of a Hindu widow, her signature or the signature of her authorised agent would be enough to bind the reversioners; so also that of a manager or Karta of a Joint Hindu family; his signature or that of his duly authorised agent will be enough to bind the other members of the family (ibid). Notice, however, that joint contractors, partners, co-executors and co-mortgagees are not, by themselves, necessarily, agents for their compeers for signing an acknowledgment of liability.

The sec. lays down the effect of an "acknowledgment of liability" by the party liable before limitation has expired. Such acknowledgment gives a fresh start for limitation. For this, however, the "acknowledgment" must (i) be in writing, (ii) it must be signed by the party or his authorised agent, and (iii) it must be made before the period of limitation has expired. Notice that "authorised agent" here is specially defined.

The acknowledgment may be in any form, e.g. a letter, a "samadaskat book", an admission in a affidavit or even a mention in a balance sheet. Denial of a debt or a plea of satisfaction is not an "acknowledgment". A promise to pay is not necessary. It need not also mention the exact amount. The Off. Assignee is not an "agent" of the debtor nor a Receiver of the debtor's property, unless specially authorised. It has been recently held in Madras, however, that as all property of the insolvent vests in the Official Assignee, an acknowledgment given by the Official Assignee will save limitation. *Ramgopal v. Muthukrishna*, 69 M.L.J. 724. An endorsement of payment on a promissory note, if signed by the debtor, would amount to an acknowledgment. An oral acknowledgment is of no effect.

Effect of part payment

Under sec. 20 as now amended, if any part payment on account of a debt (or any interest in respect of a legacy) is made by the person liable before the expiry of limitation, a fresh period of limitation will start from the date of such payment.

A special rule prevails as regards payment of interest made before 1 Jan. 1928. Acknowledgments of these payments of interest, in order to be effective, must appear in the handwriting of or in a writing signed by the person paying or his duly authorised agent.

Under the sec. as it is now amended, part payment need not appear in the handwriting of the person paying nor is his signature required. The part payment may be for interest or principal or both. For "agents", the same rules as are laid down by sec. 19 apply.

In case of a mortgage with possession, receipt of rent or produce by the mortgagee will be regarded as "part payment" under the sec. (ibid).

Addition of new party: Where a new party is added to a suit, either as plaintiff or defendant, the suit against such party shall be deemed to be instituted when he is so added (sec. 22). This rule does not apply where interest of a party to a suit, devolves on another by act of parties or operation of law during the continuance of the suit (ibid).

Continuing breaches: In case of a continuing breach of contract or any other civil liability (e.g. a nuisance, obstruction of a public right of way), limitation starts at every moment during the time the breach continues (sec. 23).

Special damage: Where a suit for compensation for a wrong cannot be filed before special damage has accrued, limitation will commence from the time such damage accrues (sec. 24).

Thus where sub-soil rights are injured, limitation will commence not from the time when such rights are invaded but from the time injury results from such invasion (ibid).

Gregorian calendar: In all computation of periods of limitation, the Gregorian calendar (and not the Lunar Calendar) shall be followed (sec. 25).

Prescription

Limitation operates as a bar to a suit, i.e. it prevents a right being enforced. It, however, does not extinguish the right. The right can be claimed as a defence, though barred by limitation. Prescription *not only bars the remedy but also extinguishes the right. Sometimes, it also confers a right.* Thus prescription may be (a) *extinctive* as well as (b) *acquisitive*. Both these aspects of prescription are provided for by secs. 26 and 28 of the Limitation Act.

Prescriptive right to easement: Under sec. 26, where access and use of light or air to and for a building have been (i) peaceably (ii) enjoyed therewith (iii) as an easement and (iv) as of right (v) without interruption (vi) for 20 years, the right to such access and use of light and air, shall become absolute and indefeasable. (vii) The period of 20 years must have expired within two years of a suit to establish such right. The same rule operates as to any easement of right of way, or of water course, or of use of water or of any other easement. Twenty years' free, open and uninterrupted user, as of right and as an easement, makes the right absolute and indefeasable (ibid). As against the Government the period is 60 years (ibid). Nothing is an obstruction of such user unless the interruption is acquiesced in by the claimant for one year after notice of the obstruction and of the person making the same (ibid). Where the subject-matter over which easement is claimed, is held by a person having a life interest therein or an interest exceeding three years, the period during which the subject-matter is so held, shall be excluded from the 20 years' period, provided the easement is resisted within 3 years of the interest ceasing (sec. 27).

The above secs. which deal with prescriptive rights to easements, e.g. of light and air through windows of a building as well as all other easements, make such rights absolute and complete, on the conditions of the secs. being satisfied. Notice that before the right can be so complete, the secs. require the claimant, as a condition precedent, to file a suit in a Court of law within 2 years after the right matures, to establish the right claimed by him.

Prescriptive right to property: Under sec. 28, where a suit for possession of any property becomes barred as a result of limitation period running out, the right and title of the person in possession of such property becomes absolute and the true owner's right thereto will be extinguished.

The sec. has the effect of conferring title on a person in adverse possession of property belonging to another on the period of limitation elapsing. Notice that the sec. applies only to property (both moveable and immovable). It does not apply to debts.

Savings: (i) The present Limitation Act does not affect the provisions of sec. 25 of the Contract Act or the Indian Divorce Act. (ii) Where any special or local law prescribes a different period of limitation, suits etc. filed after expiry of such period will be automatically dismissed. Sec. 7 and secs. 9-18 and sec. 22 of the Limitation Act (see above) shall apply in such cases only so far as they are not excluded by the provisions of the special or local law. Further the remaining secs. of the Limitation Act shall not apply at all in such cases. (iii) As regards Part B States (in which the Limitation Act is not made applicable), if the corresponding period of limitation prescribed by their Limitation Law is longer than that prescribed by the present Limitation Act, the suits in such States must be filed within 2 years of the present Limitation Act being extended to them or their original period of limitation, whichever expires first (secs. 29-39).

Some important periods of limitation for filing suits of a mercantile nature are given below from the Schedule to the Act.

THE FIRST SCHEDULE

SUITS

Description of suit.	Period of Limitation.	Time from which period begins to run.
6.—Upon a Statute, Act, Regulation, or Bye-law, for a penalty or forfeiture.	One year	When the penalty or forfeiture is incurred.
7.—For the wages of a household servant, artisan, or labourer.	One year	When the wages accrue due.
8.—For the price of food or drink sold by the keeper of a hotel, tavern or lodging-house.	One year	When the food or drink is delivered.
9.—For the price of lodging.	One year	When the price becomes payable.
27.—For compensation for inducing a person to break a contract with the plaintiff.	One year	The date of the breach.
30.—Against a carrier for compensation for losing or injuring goods.	One year	When the loss or injury occurs.
31.—Against a carrier for compensation for non-delivery of, or delay in delivering goods.	One year	When the goods ought to be delivered.
32.—Against one who, having a right to use property for specific purposes, perverts it to other purposes.	Two years	When the perversion first becomes known to the person injured thereby.
36.—For compensation for any malfeasance, misfeasance, or non-feasance independent of contract, and not herein specially provided for.	Two years	When the malfeasance, misfeasance, or non-feasance takes place.
48.—For specific moveable property lost, or acquired by theft, or dishonest misappropriation or conversion, or for compensation for wrongfully taking or detaining the same.	Three years	When the person having the right to the possession of the property first learns in whose possession it is.
48A.—To recover moveable property conveyed or bequeathed in trust, deposited or pawned and afterwards bought from the trustee, depository or pawnee for a valuable consideration.	Three years	When the sale becomes known to the Plaintiff.
49.—For other specific moveable property, or for compensation for wrongfully taking or injuring or wrongfully detaining the same.	Three years	When the property is wrongfully taken or injured, or when the detainer's possession becomes unlawful.
50.—For the hire of animals, vehicles, boats, or household furniture.	Three years	When the hire becomes payable.
51.—For the balance of money advanced in payment of goods to be delivered.	Three years	When the goods ought to be delivered.
52.—For the price of goods sold and delivered, where no fixed period of credit is agreed upon.	Three years	The date of the delivery of the goods.
53.—For the price of goods sold and delivered to be paid for after the expiry of a fixed period of credit.	Three years	When the period of credit expires.
54.—For the price of goods sold and delivered to be paid for by a bill of exchange, no such bill being given.	Three years	When the period of the proposed bill elapses.

Description of suit.	Period of Limitation.	Time from which period begins to run.
56.—For the price of work done by the plaintiff for the defendant at his request, where no time has been fixed for payment.	Three years	When the work is done.
57.—For money payable for money lent.	Three years	When the loan is made.
58.—Like suit when the lender has given a cheque for the money.	Three years	When the cheque is paid.
59.—For money lent under an agreement that it shall be payable on demand.	Three years	When the loan is made.
60.—For money deposited under an agreement that it shall be payable on demand, including money of a customer in the hands of his banker so payable.	Three years	When the demand is made.
61.—For money payable to the plaintiff for money paid for the defendant.	Three years	When the money is paid.
62.—For money payable by the defendant to the plaintiff for money received by the defendant for the plaintiff's use.	Three years	When the money is received.
63.—For money payable for interest upon money due from the defendant to the plaintiff.	Three years	When the interest becomes due.
64.—For money payable to the plaintiff for money found to be due from the defendant to the plaintiff on accounts stated between them.	Three years	When the accounts are stated in writing signed by the defendant or his agent duly authorized in this behalf, unless where the debt is, by a simultaneous agreement in writing signed as aforesaid, made payable at a future time and then when that time arrives.
65.—For compensation, for breach of a promise to do anything at a specified time, or upon the happening of a specified contingency.	Three years	When the time specified arrives or the contingency happens.
66.—On a single bond, where a day is specified for payment.	Three years	The day so specified.
67.—On a single bond, where no such day is specified.	Three years	The date of executing the bond.
68.—On a bond subject to a condition.	Three years	When the condition is broken.
69.—On a bill of exchange or promissory note payable at a fixed time after date.	Three years	When the bill or note falls due.
70.—On a bill of exchange payable at sight or after sight, but not at a fixed time.	Three years	When the bill is presented.
71.—On a bill of exchange accepted payable at a particular place.	Three years	When the bill is presented at that place.
72.—On a bill of exchange or promissory note payable at a fixed time after sight or after demand.	Three years	When the fixed time expires.
73.—On a bill of exchange or promissory note payable on demand and not accompanied by any writing restraining or postponing the right to sue.	Three years	The date of the bill or note.
74.—On a promissory note or bond payable by instalments.	Three years	The expiration of the first term of payment as to the part then payable; and for the other parts, the expiration of the respective terms of payment.

Description of suit.	Period of Limitation.	Time from which period begins to run.
75.—On a promissory note or bond payable by instalments, which provides that, if default be made in payment of one or more instalments, the whole shall be due.	Three years	When the default is made unless where the payee or obligee waives the benefit of the provision, and then when fresh default is made in respect of which there is no such waiver.
76.—On a promissory note given by the maker to a third person to be delivered to the payee after a certain event should happen.	Three years	The date of the delivery to the payee.
77.—On a dishonoured foreign bill, where protest has been made and notice given.	Three years	When the notice is given.
78.—By the payee against the drawer of a bill of exchange which has been dishonoured by non-acceptance.	Three years	The date of the refusal to accept.
79.—By the acceptor of an accommodation-bill against the drawer.	Three years	When the acceptor pays the amount of the bill.
80.—Suit on a bill of exchange, promissory note, or bond not herein expressly provided for.	Three years	When the bill, note, or bond becomes payable.
81.—By a surety against the principal debtor.	Three years	When the surety pays the creditor.
82.—By a surety against a co-surety.	Three years	When the surety pays anything in excess of his own share.
83.—Upon any other contract to indemnify	Three years	When the plaintiff is actually damaged.
85.—For the balance due on a mutual, open, and current account, where there have been reciprocal demands between the parties.	Three years	The close of the year in which the last item admitted or proved is entered in the account; such year to be computed as in the account.
86.—(a) On a policy of insurance, when the sum assured is payable after proof of the death has been given to or received by insurers.	Three years	The date of the death of the deceased.
(b) On a policy of insurance, when the sum insured is payable after proof of the loss has been given to or received by the insurers.	Three years	The date of the occurrence causing the loss.
87.—By the assured to recover premia paid under a policy voidable at the election of the insurers.	Three years	When the insurers elect to avoid the policy.
88.—Against a factor for an account.	Three years	When the account is, during the continuance of the agency, demanded and refused, or, where no such demand is made, when the agency terminates.
89.—By a principal against his agent for moveable property received by the latter and not accounted for.	Three years	When the account during the continuance of the agency, is demanded and refused or where no such demand is made, when the agency terminates.
90.—Other suits by principals against agents for neglect or misconduct.	Three years	When the neglect or misconduct becomes known to the plaintiff.

Description of suit.	Period of Limitation.	Time from which period begins to run.
96.—For relief on the ground of mistake.	Three years	When the mistake becomes known to the Plaintiff. The date of the failure.
97.—For money paid upon an existing consideration which afterwards fails.	Three years	
98.—To make good out of the general estate of a deceased trustee the loss occasioned by a breach of trust.	Three years	The date of the trustee's death, or if the loss has not then resulted, the date of the loss.
100.—By a co-trustee to enforce against the estate of a deceased trustee a claim for contribution.	Three years	When the right to contribution accrues.
101.—For a seaman's wages.	Three years	The end of the voyage during which the wages are earned. When the wages accrue due.
102.—For wages not otherwise expressly provided for by this Schedule.	Three years	
105.—By a mortgagor after the mortgage has been satisfied, to recover surplus collections received by the mortgagees.	Three years	When the mortgagor re-enters on the mortgaged property.
106.—For an account and a share of the profits of a dissolved partnership.	Three years	The date of the dissolution.
110.—For arrears of rent.	Three years	When the arrears become due.
112.—For a call by a company registered under any Statute or Act.	Three years	When the call is payable.
113.—For specific performance of a contract.	Three years	The date fixed for the performance, or, if no such date is fixed, when the plaintiff has notice that performance is refused.
114.—For the rescission of a contract.	Three years	When the facts entitling the plaintiff to have the contract rescinded first become known to him.
115.—For compensation for the breach of any contract, express or implied, not in writing registered, and not herein specially provided for.	Three years	When the contract is broken, or (where there are successive breaches) when the breach in respect of which the suit is instituted occurs, or (where the breach is continuing) when it ceases.
116.—For compensation for the breach of a contract in writing registered.	Six years	When the period of limitation would begin to run against a suit brought on a similar contract not registered.
120.—Suit for which no period of limitation is provided elsewhere in this Schedule.	Six years	When the right to sue accrues.
132.—To enforce payment of money charged upon immoveable property.	Twelve years	When the money sued for becomes due.

Explanation.—For the purposes of this article, (a) allowances and fees respectively, called malikana and haqqe and (b) the value of any agricultural or other produce, the right to receive which is secured by a charge upon immoveable property and (c) advances secured by mortgage by deposit of title deeds, shall be deemed to be money charged upon immoveable property.

Description of suit.	Period of Limitation.	Time from which period begins to run.
134.—To recover possession of immoveable property conveyed or bequeathed in trust, or mortgaged and afterwards transferred by the trustee or mortgagee for a valuable consideration.	Twelve years	When the transfer becomes known to the Plaintiff.
134(A).—To set aside a transfer of immoveable property comprised in a Hindu, Muhammadan or Buddhist religious or charitable endowment made by a manager thereof for a valuable consideration.	Twelve years	When the transfer becomes known to the Plaintiff.
134(B).—By the manager of a Hindu, Muhammadan or Buddhist religious or charitable endowment to recover possession of immoveable property comprised in the endowment which has been transferred by a previous manager for a valuable consideration.	Twelve years	The death, resignation or removal of the transferor.
134(C).—By the manager of a Hindu, Muhammadan or Buddhist religious or charitable endowment to recover possession of moveable property comprised in the endowment which has been sold by a previous manager for a valuable consideration.	Twelve years	The death, resignation or removal of the seller.
135.—Suit instituted in a Court not established by Royal Charter by a mortgagee for possession of immoveable property mortgaged.	Twelve years	When the mortgagor's right to possession determines.
145.—Against a depository or pawnee to recover moveable property deposited or pawned.	Thirty years	The date of the deposit or pawn.
146.—Before a Court established by Royal Charter in the exercise of the ordinary original civil jurisdiction by mortgagee to recover from the mortgagor the possession of immoveable property mortgaged.	Thirty years	When any part of the principal or interest was last paid on account of the mortgage debt.
147.—By a mortgagee for foreclosure or sale.	Sixty years	When the money secured by the mortgage becomes due.
148.—Against a mortgagee to redeem or to recover possession of immoveable property mortgaged.	Sixty years	When the right to redeem or to recover possession accrues: Provided that all claims to redeem arising under instruments of mortgage of immoveable property situate in Lower Burma which had been executed before the first day of May 1863, shall be governed by the rules of limitation in force in that province immediately before the same day.

CHAPTER XXI

STAMP

The Stamp Act: The Act (2 of 1899) lays down the law regarding liability of instruments to stamp duty. The Act extends to the whole of India. It is a fiscal Act and is construed strictly against the revenue authority.

Definitions: In this Act, certain definitions are important. They are as follows (sec. 2):

- (1) **"Banker"** includes a bank and any person acting as a banker.
- (2) **"Bill of Exchange"** means a bill of exchange as defined by the Negotiable Instruments Act, 1881, and includes also a hundi and any other document entitling or purporting to entitle any person, whether named therein or not, to payment by any other person of, or to draw upon any other person for, any sum of money.
- (3) **"Bill of exchange payable on demand"** includes: (a) an order for the payment of any sum of money by a bill of exchange or promissory note, or for the delivery of any bill of exchange or promissory note in satisfaction of any sum of money, or for the payment of any sum of money out of any particular fund which may or may not be available, or upon any condition or contingency which may or may not be performed or happen; (b) an order for the payment of any sum of money weekly, monthly, or at any other stated periods; and (c) a letter of credit, that is to say, any instrument by which one person authorises another to give credit to the person in whose favour it is drawn.
- (4) **"Bill of Lading"** includes a "through bill of lading", but does not include a mate's receipt.
- (5) **"Bond"** includes: (a) any instrument whereby a person obliges himself to pay money to another on condition that the obligation shall be void if a specified act is performed, or is not performed, as the case may be; (b) any instrument attested by a witness, and not payable to order or bearer, whereby a person obliges himself to pay money to another; and (c) any instrument so attested, whereby a person obliges himself to deliver grain or other agricultural produce to another.
- (6) **"Cheque"** means a bill of exchange drawn on a specified banker, and not expressed to be payable otherwise than on demand.
- (7) **"Mortgage-deed"** includes every instrument whereby, for the purpose of securing money advanced, or to be advanced, by way of loan, or an existing or future debt, or the performance of an engagement, one person transfers or creates, to or in favour of another, a right over, or in respect of, specified property.
- (8) **"Policy of insurance"** includes: (a) any instrument by which one person, in consideration of a premium, engages to indemnify another against loss, damages, or liability arising from an unknown or contingent event; (b) a life-policy, and any policy insuring any person against accident or sickness and any other personal insurance.
- (9) **"Policy of sea-insurance" or "sea-policy"** means (a) any insurance made upon any ship or vessel (whether for marine or inland navigation), or upon the machinery, tackle, or furniture of any ship or vessel, or upon any goods, merchandise, or property of any description whatever on board of any ship or vessel, or upon the freight of, or any other interest which may be lawfully insured in or relating to, any ship or vessel, and (b) includes any insurance of goods, merchandise, or property for any transit which includes, not only a sea-risk within the meaning of clause (a), but also any other risk incidental to the transit insured from the commencement of the transit to the ultimate destination covered by the insurance.

Where any person, in consideration of any sum of money paid or to be paid for additional freight or otherwise, agrees to take upon himself any risk attending goods, merchandise, or property of any description whatever while on board of any ship or

vessel, or engages to indemnify the owner of any such goods, merchandise, or property from any risk, loss or damage, such agreement or engagement shall be deemed to be a contract for sea-insurance.

(10) "Power-of-attorney" includes any instrument (not chargeable with a fee under the law relating to court-fees for the time being in force) empowering a specified person to act for, and in the name of, the person executing it.

(11) "Promissory note" means a promissory note as defined by the Negotiable Instruments Act, 1881; it also includes a note promising the payment of any sum of money out of any particular fund which may or may not be available or upon any condition or contingency which may or may not be performed or happen.

(12) "Receipt" includes any note, memorandum, or writing (a) whereby any money, or any bill of exchange, cheque, or promissory note is acknowledged to have been received, or (b) whereby any other moveable property is acknowledged to have been received in satisfaction of a debt, or (c) whereby any debt or demand, or any part of a debt or demand, is acknowledged to have been satisfied or discharged, or (d) which signifies or imports any such acknowledgment, and whether the same is or is not signed with the name of any person.

Instruments liable to stamp duty

Under sec. 3 of the Act: (i) instruments mentioned in Sch. I and executed in India (except Part B States) after 1 July 1893, (ii) Bills of Exchange (payable otherwise than on demand) and promissory notes made out of India (except Part B States) after the above date and acted upon in India, i.e. accepted, paid, transferred, otherwise negotiated in India, (iii) and other instruments [excluding (i) and (ii)] mentioned in Sch. I executed out of India (except Part B States) after the above date and relating to property situate or anything done in India (except Part B States) and received in India (except Part B States), are liable to stamp duty.

No duty is chargeable, however, on instrument: (i) in favour of Government, (ii) sales, mortgages and other dispositions of a ship or vessel registered under the Merchant Shipping Act, Indian Registration of Ships Act or Bombay Coasting Vessels Act (sec. 3); (iii) in favour of the Off. Ass. (sec. 115, Presidency Towns Insolvency Act); (iv) in favour of local authority (sec. 18). If more than one instrument is employed with regard to a transaction, the principal instrument alone is chargeable with the full duty, and the rest with a duty of not more than Re. 1.

Notice that under sec. 7, no contract of sea insurance is valid unless it is expressed in a sea policy. Further, no time sea policy can extend to beyond 12 months (without a fresh policy for the excess) (*ibid*). No sea policy is also valid, unless it specifies the particular risk or adventure, and the time for which it is made, the names of the underwriters and the amount. A mixed policy (time and voyage policy) and a voyage policy extending beyond 30 days after safe arrival of vessels shall be stamped as a combined time and voyage policy.

Instruments, how to be stamped

Generally all instruments chargeable with duty, have to be stamped with impressed stamps, i.e. stamp paper on which the required stamp is embossed or engraved. In some cases however "adhesive stamps" (i.e. revenue stamps) are permitted. These are: (i) instruments chargeable with duty of one (or half) anna (except parts of bills in sets not payable otherwise than on demand); (ii) promissory notes and bills of exchange drawn or made out of India (except Part B States); (iii) entry of vakil or advocate on the Rolls; (iv) notarial acts; (v) transfers by endorsements of shares in incorporated companies (sec. 11). Adhesive stamps must always be cancelled at the time of use (sec. 12). In certain special cases coloured impressions and impressed labels are also permitted to be used.

Instruments executed in India should be stamped at or before their execution (sec. 17). Instruments (other than Bills of Exchange and promissory notes) executed outside India (except Part B States) must be stamped within 3 months of their first

receipt in India (except Part B States). Bills of Exchange and promissory notes executed outside India (except Part B States) must be stamped before presenting them for acceptance or payment or negotiation in India (secs. 18-19).

Generally the person executing the instrument has to pay the stamp duty except in case of a conveyance or lease when the purchaser or lessee respectively has to pay the same. In partition all parties pay according to their respective shares (sec. 29).

Consequences of not stamping instruments (secs. 33-36)

- (i) Such instruments can be impounded (sec. 33).
- (ii) In case of unstamped receipts, proper stamped receipts may be required to be substituted (sec. 34).
- (iii) Unstamped instruments cannot be admitted in evidence "for any purpose" or be acted upon, or registered by any public officer. "Unstamped" here includes under-stamped also. "For any purpose" has been construed by the Privy Council to include a collateral purpose also. *Ram Ratan v. Parma Nanda*, 73 I.A. 28.

To (iii) there are certain exceptions (sec. 35):

- (a) instruments not duly stamped [excepting bills of exchange, promissory notes and instruments chargeable with duty of one anna (or half anna)], can be admitted in evidence on payment of proper duty, together with a penalty of Rs. 5 or ten times the value of proper duty, where the same exceeds Rs. 5;
- (b) an unstamped receipt can be used against the person giving it on payment of Re. 1 as penalty;
- (c) instruments not duly stamped can be admitted in criminal trials;
- (d) if such instruments are certified by the Collector, as provided by the Act, they can be admitted in evidence; and
- (e) if an unstamped instrument is admitted in evidence, it cannot be challenged afterwards on that ground (sec. 36).

Duty payable on various instruments (Sch. I)

N.B.—In some of the Indian Provinces, like Bihar, Bombay, C.P. & Berar, Orissa and U.P., there exist special Acts, levying temporary surcharges, on various duties chargeable under the Act. These must be consulted wherever necessary. Bombay Act XIX of 1943 places a surcharge of 50 per cent on all duties leviable under the Act, except those leviable on bills of exchange, cheques, promissory notes, bills of lading, letters of credit, policies of insurance, proxies and receipt.

1. **ACKNOWLEDGMENT** of a debt exceeding twenty rupees in amount or value, written or signed by, or on behalf of, a debtor in order to supply evidence of such debt in any book (other than a banker's pass-book), or on separate piece of paper, when such book or paper is left in the creditor's possession: provided that such acknowledgment does not contain any promise to pay the debt, or any stipulation to pay interest, or to deliver any goods or other property: *One anna*.

Local Acts: Bihar, C.P. & Berar: *Two annas*.

4. **AFFIDAVIT** :, including an affirmation or declaration in the case of persons by law allowed to affirm or declare instead of swearing: *One rupee*.

Exemptions: Affidavit or declaration in writing when made:—

(a) as a condition of enrolment under the Indian Army Act, 1911, or the Indian Air Force Act, 1932; (b) for the immediate purpose of being filed or used in any Court, or before the officer of any Court; or (c) for the sole purpose of enabling any person to receive any pension or charitable allowance.

Local Acts: Bengal, Bombay, Burma, Bihar, C.P. & Berar, Madras, Punjab: *Two rupees*.

5. AGREEMENT OR MEMORANDUM OF AN AGREEMENT:—

- (a) if relating to the sale of a bill of exchange: *Two annas.*
- (b) if relating to the sale of a Government security or share in an incorporated Company, or other body corporate: *Subject to a maximum of ten rupees, one anna for every Rs. 10,000 or part thereof of the value of the security or share.*
- (c) if not otherwise provided for: *Eight annas.*

Exemptions: Agreement or Memorandum of Agreement:—(a) for or relating to the sale of goods or merchandise exclusively, not being a Note or Memorandum chargeable under No. 43; (b) made in the form of tenders to the Central Government for or relating to any loan; (c) made under the European Vagrancy Act, 1874, section 17.

Local Acts: Bombay: (a) If relating to a sale of a bill of exchange: *Four annas*; (aa) if relating to purchase or sale of government security, subject to a maximum of Rs. 20, Two annas for every Rs. 10,000 or part thereof, of the value of the security at the time of its purchase or sale, as the case may be; (b) if relating to purchase or sale of share, scrips, bonds, debentures, debenture stock or any other marketable security of a like nature in or of any incorporate company or other body: *Two annas* for every Rs. 2,500 or part thereof, of the value of the security at the time of its purchase or sale as the case may be; (c) if not otherwise provided for: *One rupee.*

Exemptions: Agreement or memorandum of agreement (a) for the purchase or sale of goods or merchandise exclusively, not being a note or memorandum chargeable under No. 43; (b) made in the form of tenders to the Central Government for or relating to any loan; (c) made under the European Vagrancy Act, 1874, sec. 17; (d) made in respect of purchase or sale of a Government security or of a share, scrip, stock, bond, debenture, debenture stock, or other marketable security of a like nature in or of any incorporated company or other body corporate, an entry relating to which is required to be made in a clearance list in accordance with the rules of a stock exchange recognised under the Bombay Security Contracts Control Act, 1925.

Madras, Bihar, C.P. and Berar, U.P.: (a) 3 annas; (b) subject to maximum of Rs. 15, one and one half anna for every Rs. 10,000 or part thereof, of the value of the security or share; (c) Twelve annas. **Punjab, Burma, Bengal:** *Punjab:* (a) Four annas; (b) subject to maximum of Rs. 15, Two annas for every Rs. 10,000 or part thereof, of the value of the security or share; (c) One rupee. *Burma:* (a) Four annas; (b) subject to maximum of Rs. 20, Two annas for Rs. 10,000 or part thereof of the value of the security or share; (c) One rupee. *Bengal:* (a) Four annas; (b) subject to maximum of Rs. 20, Two annas for every Rs. 10,000 or part thereof if relating to sale of Government security; Two annas for every Rs. 5,000 or part thereof, if relating to sale of share in a body corporate; (c) One rupee.

6. AGREEMENT RELATING TO DEPOSIT OF TITLE DEEDS, PAWN, OR PLEDGE, that is to say, any instrument evidencing an agreement relating to:—(1) the deposit of title-deeds or instruments constituting or being evidence of the title to any property whatever (other than a marketable security), or (2) the pawn, or pledge of moveable property, where such deposit, pawn, or pledge has been made by way of security for the repayment of money advanced or to be advanced by way of loan or an existing or future debt:—

- (a) if such loan or debt is repayable on demand or more than three months from the date of the instrument evidencing the agreement: *The same duty as a Bill of Exchange [No. 13(b)] for the amount secured;*
- (b) if such loan or debt is repayable not more than three months from the date of such instrument: *Half the duty payable on a Bill of Exchange [No. 13(b)] for the amount secured.*

Exemption: Instrument of pawn or pledge of goods if unattested.

Local Acts: (a) *Bengal, Madras, Punjab:* (i) where amount of loan or debt does not exceed Rs. 200, Rs. 0-4-6; (ii) for every additional Rs. 200 or part thereof, upto

Rs. 3,000, same rate; (iii) for every additional Rs. 10,000 or part thereof, thereafter, Rs. 13-8-0. *Bihar, C.P. & Berar*: (i) where amount of debt or loan does not exceed Rs. 100, Rs. 0-3-0; (ii) where it does not exceed Rs. 200, Rs. 0-4-6; (iii) for every additional Rs. 200 or part thereof, upto Rs. 7,500, same rate; (iv) where it exceeds Rs. 7,500, but does not exceed Rs. 10,000, Rs. 13-8-0; (v) for every additional Rs. 5,000 or part thereof, upto Rs. 30,000, Rs. 6-12-0; (vi) for every additional Rs. 10,000 or part thereof in excess, Rs. 13-8-0. *U.P.*: (i) Where amount of loan or debt does not exceed Rs. 200, Rs. 0-3-0; (ii) where it does not exceed Rs. 400, Rs. 0-8-0; (iii) for every additional Rs. 200 or part thereof, thereafter, upto Rs. 30,000, Rs. 0-4-0; (iv) for every additional Rs. 10,000 or part thereof, exceeding Rs. 30,000, Rs. 12-0-0.

(b) *Bengal, Madras, Punjab*: Half the duty payable on loan or debt under clause (a) (i) or clause (a) (ii) for the amount secured. *Bihar, C.P. & Berar*: Half the duty payable on loan or debt under clause (a) (i) or clause (a) (ii) or clause (a) (iii) for the amount secured. *U.P.*: If such loan or debt is repayable not more than 3 months from date of instrument, half the duty on debt or loan under clause (a) for amount secured.

9. **APPRENTICE DEED**: Including every writing relating to the service or tuition of any apprentice, clerk or servant, placed with any master to learn any profession, trade or employment, not being articles of clerkship (No. 11): *Five rupees*.

Exemption: Instruments of apprenticeship executed by a Magistrate under the Apprentice Act, 1850, or by which a person is apprenticed by or at the charge of any public charity.

Local Acts: *Madras, Bihar, C.P. & Berar, Burma, U.P.*: Rs. 7-8-0. *Bombay, Bengal*: Rs. 10.

10. **ARTICLES OF ASSOCIATION OF A COMPANY**: *Twenty-five rupees*.

Exemption: Articles of any Association not formed for profit, and registered under section 26 of the Indian Companies Act, 1882.

Local Acts: *Bombay, Burma*: (a) Where the Company has no share capital or the nominal share capital does not exceed Rs. 2,500, Rs. 25; (b) where the nominal share capital exceeds Rs. 2,500 but does not exceed Rs. 100,000, Rs. 50; (c) where the nominal share capital exceeds Rs. 100,000, Rs. 100. *Madras*: Rs. 50. *Bihar, C.P. & Berar*: Rs. 50. *Punjab*: (i) Where authorised capital does not exceed Rs. 1 lakh, Rs. 25; (ii) in other cases, Rs. 50. *Bengal*: (i) Where nominal capital does not exceed Rs. 1 lakh, Rs. 50; (ii) in other cases, Rs. 100.

11. **ASSIGNMENT**: See **CONVEYANCE**.

12. **AWARD**: that is to say, any decision in writing by an arbitrator or umpire, not being an award directing partition, on a reference made otherwise than by an order of the Court, in the course of a suit (a) where the amount or value of the property to which the award relates as set forth in such award, does not exceed Rs. 1,000, the same duty as a Bond (No. 15) for such amount: (b) in any other case, *Five rupees*.

Exemption: Award under the Bombay District Municipal Act, 1873, sec. 81, or the Bombay Hereditary Officers' Act, 1874, sec. 18.

Local Acts: *Bombay*: Clauses (a) and (b) omitted: same duty as a bond (No. 15) for the amount or value of the property to which the award relates as set forth in such award, subject to a maximum of Rs. 20. *Punjab, Bihar, C.P. & Berar, U.P.*: (a) Where the amount or the value of the property to which award relates as set forth therein does not exceed Rs. 1,000: same duty as a bond (No. 15) for such amount; (b) where it exceeds Rs. 1,000 but not Rs. 5,000: Rs. 7-8-0; for every additional Rs. 1,000 or part thereof in excess of Rs. 5,000, Rs. 0-8-0, subject to a maximum of Rs. 50. (U.P. omits maximum.) *Bengal*: (b) Where it exceeds Rs. 1,000 but not Rs. 5,000: Rs. 10; for every additional Rs. 1,000 or part thereof, in excess of Rs. 1,000,

Rs. 0-8-0, subject to a maximum of Rs. 50. *Madras*: (a) Where amount or value of property to which award relates as set forth therein does not exceed Rs. 1,000: same duty as bottomry bond (No. 16) for such amount; (b) where it exceeds Rs. 1,000, but not Rs. 5,000: Rs. 10; for every additional Rs. 1,000 or part thereof in excess of Rs. 5,000: Rs. 0-8-0, with a maximum of Rs. 50. *Burma*: (a) Where value or amount of property as set forth in the award does not exceed Rs. 1,000: Rs. 0-8-0 for every Rs. 100 or part thereof, subject to a maximum of Rs. 2-8-0; (b) where it exceeds Rs. 1,000 but not Rs. 1,500: Rs. 7-8-0; (c) where it exceeds Rs. 1,500, but not Rs. 2,000: Rs. 10; (d) for every additional Rs. 500 or part thereof above Rs. 2,000: Re. 1, subject to a maximum of Rs. 50.

13. **BILL OF EXCHANGE** [as defined by Act] not being a Bond, bank-note, or currency-note; (if drawn singly):—

(b) where payable otherwise than on demand, but not more than one year after date or sight:—

(i) if the amount of the bill or note does not exceed Rs. 200: Rs. 0-3-0; (ii) for every additional Rs. 200 or part thereof, not exceeding Rs. 30,000: Rs. 0-3-0; (iii) for every additional Rs. 10,000 or part thereof, in excess of Rs. 30,000: Rs. 9.

N.B.—If drawn in a set of two $\frac{1}{2}$ duty on each part; if drawn in a set of three, $\frac{1}{3}$ rd duty on each part.

(c) where payable at more than one year after date or sight: *The same duty as a Bond (No. 15) for the same amount.*

14. **BILL OF LADING** (including a through bill of lading): *Four annas.*

N.B.—If a bill of lading is drawn in parts, the proper stamp therefor must be borne by each one of the set.

Exemptions: (a) Bill of lading when the goods therein described as received at a place within the limits of any ports as defined under the Indian Ports Act, 1889, and are to be delivered at another place within the limits of the same port. (b) Bill of lading when executed out of British India, and relating to property to be delivered in British India.

Local Acts: *Bengal, Burma, Madras:* Six annas; *Punjab:* Eight annas.

15. **BOND** [as defined by Act (5)] not being a Debenture (No. 27) and not being otherwise provided for by this Act or by the Court Fees Act, 1870:—

(i) where the amount or value secured does not exceed Rs. 10: *Two annas*; (ii) where it exceeds Rs. 10, and does not exceed Rs. 50: *Four annas*; (iii) for every additional Rs. 50, or part thereof, upto Rs. 1,000, *Four annas*; (iv) for every Rs. 500, or part thereof, in excess of Rs. 1,000, Rs. 2-8-0.

Exemptions: Bond, when executed by—

(a) headmen nominated under rules framed in accordance with the Bengal Irrigation Act, 1876, section 99, for the due performance of their duties under that Act, (b) any person for the purpose of guaranteeing that the local income derived from private subscriptions to charitable dispensary or hospital or any other object of public utility, shall not be less than a specified sum per mensem.

Local Acts:

(i) Where it exceeds Rs. 50 but does not exceed Rs. 100: *Bihar:* Rs. 0-10-0. (ii) Where it exceeds Rs. 100 but not Rs. 200: *Madras, Bihar, Burma:* Rs. 1-4-0. (iii) Where it exceeds Rs. 200 but not Rs. 300: *Bengal, Madras, Punjab:* Rs. 1-14-0; *Bombay, Bihar, Burma:* Rs. 2-4-0; *U.P.:* Rs. 1-10-0. (iv) Where it exceeds Rs. 300 but not Rs. 400: *Bihar, Bombay, Bengal, Burma:* Rs. 3; *U.P.:* Rs. 2-4-0; *Madras, Punjab, C.P. & Berar:* Rs. 2-8-0. (v) Where it exceeds Rs. 400 but not Rs. 500: *Bihar, Bombay, Bengal, Burma:* Rs. 3-12-0; *C.P. & Berar:* Rs. 3-8-0; *U.P.:* Rs. 2-14-0; *Madras, Punjab:* Rs. 3-2-0. (vi) Where it exceeds Rs. 500 but not Rs. 600: *Bengal, Madras, Rangoon, Bombay, Bihar, Burma, U.P., C.P. & Berar:* Rs. 4-8-0.

(vii) Where it exceeds Rs. 600 but not Rs. 700 : *Bengal, Madras, Punjab, Bombay, Burma, Bihar, U.P., C.P. & Berar* : Rs. 5-4-0. (viii) Where it exceeds Rs. 700 but not Rs. 800 : *Bengal, Madras, Punjab, Bombay, Burma, Bihar, U.P., C.P. & Berar* : Rs. 6-0-0. (ix) Where it exceeds Rs. 800 but not Rs. 900 : *Bengal, Madras, Punjab, Bombay, Burma, Bihar, U.P., C.P. & Berar* : Rs. 6-12-0. (x) Where it exceeds Rs. 900 but not Rs. 1,000 : *Bengal, Madras, Punjab, Bombay, Burma, Bihar, U.P., C.P. & Berar* : Rs. 7-8-0. (xi) For every Rs. 500, or part thereof over Rs. 1,000 : *Bengal, Madras, Punjab, Bombay, Burma, Bihar, U.P., C.P. & Berar* : Rs. 3-12-0.

16. **BOTTOMRY-BOND**, that is to say, any instrument whereby the master of a sea-going ship borrows money on the security of the ship to enable him to preserve the ship, or prosecute her voyage : *The same duty as a Bond (No. 15) for the same amount.*

Local Acts : Bengal, Madras, Punjab : (i) Where amount or value does not exceed Rs. 10, Rs. 0-3-0 ; (ii) where it exceeds Rs. 10 but not Rs. 50, Rs. 0-6-0 ; (iii) for every additional Rs. 50, or part thereof, not exceeding Rs. 1,000, Rs. 0-6-0 ; (iv) for every Rs. 500, or part thereof, in excess of Rs. 1,000, Rs. 3-12-0.

19. **CERTIFICATE OR OTHER DOCUMENT**, evidencing the right or title of the holder thereof or any other person either to any shares, scrip or stock in or of any incorporated company or other body corporate or to become proprietor of shares, scrip or stock in or of any such company or body : *Two annas.*
20. **CHARTER PARTY**, that is to say, any instrument (except an agreement for the hire of a tug-steamer) whereby a vessel or some specified principal part thereof is let for the specified purposes of the charter, whether it includes a penalty clause or not : *One rupee.*

Local Acts : Bengal, Bombay, Burma, Bihar, C.P. & Berar, Madras, Punjab : Rs. 2.

22. **COMPOSITION DEED**, that is to say, any instrument executed by a debtor whereby he conveys his property for the benefit of his creditors or whereby payment of a composition or dividend on their debts is secured to the creditors or whereby provision is made for the continuance of the debtor's business under the supervision of inspectors or under letters of licence for the benefit of his creditors : *Ten rupees.*

Local Acts : Punjab, U.P. : Rs. 12-8 ; *Bombay, Bengal :* Rs. 20.

23. **CONVEYANCE** (as defined by Act), not being a transfer charged or exempted under No. 62 : where the amount or value of the consideration for such conveyance as set forth therein, does not exceed Rs. 50 : *Eight annas* ; where it exceeds Rs. 50 : *One rupee*, for every hundred rupees, or part thereof, upto Rs. 1,000, and where it exceeds Rs. 1,000, for every Rs. 500 or part thereof in excess : *Five rupees.*

Exemption : Assignment of copyright made under the Indian Copyright Act, 1914, Sec. 5.

Local Acts : Madras, Bihar, C.P. & Berar, Burma : Rs. 15.

(i) Where amount or value does not exceed Rs. 50 : *Bengal, Bihar, Madras, Punjab :* 12 annas. (ii) Where it exceeds Rs. 50 but not Rs. 100 : *Bengal, Bihar, Madras, Punjab :* Re. 1-8-0. (iii) Where it exceeds Rs. 100 but not Rs. 200 : *Bengal, Bihar, Madras, Punjab :* Rs. 3 ; *Burma :* Rs. 2-8-0. (iv) Where it exceeds Rs. 200 but not Rs. 300 : *Bengal, Bombay, Bihar, Burma, Madras, Punjab :* Rs. 4-8-0 ; *U.P. :* Rs. 3-4-0 ; *C.P. & Berar :* Rs. 3-8-0. (v) Where it exceeds Rs. 300 but not Rs. 400 : *Bengal, Bombay, Bihar, Burma, Madras, Punjab :* Rs. 6 ; *U.P. :* Rs. 4-8-0 ; *C.P. & Berar :* Rs. 5-8-0. (vi) Where it exceeds Rs. 400 but not Rs. 500 : *Bengal, Bombay, Bihar, Burma, Madras, Punjab, C.P. & Berar :* Rs. 7-8-0 ; *U.P. :* Rs. 5-12-0. (vii) Where it exceeds Rs. 500 but not Rs. 600 : *Bengal, Bombay, Bihar, Burma, Madras, Punjab, C.P. & Berar, U.P. :* Rs. 9. (viii) Where it exceeds Rs. 600 but not Rs. 700 : *Bengal, Bombay, Bihar, Burma, Madras, Punjab, C.P. & Berar, U.P. :* Rs. 10-8-0. (ix) Where it exceeds Rs. 700 but not Rs. 800 : *Bengal, Bombay, Bihar, Burma, Madras, Punjab, C.P. & Berar, U.P. :* Rs. 12. (x) Where it exceeds Rs. 800 but not Rs. 900 : *Bengal, Bombay, Bihar, Burma, Madras, Punjab, C.P. & Berar, U.P. :* Rs.

13-8-0. (xi) Where it exceeds Rs. 900 but not Rs. 1,000: *Bengal, Bombay, Bihar, Burma, Madras, Punjab, C.P. & Berar, U.P.*: Rs. 15. (xii) For every Rs. 500, or part thereof, exceeding Rs. 1,000: *Bombay, Bengal, Burma, Bihar, Madras, Punjab, C.P. & Berar, U.P.*: Rs. 7-8-0.

Bombay City: (i) Where it exceeds Rs. 200 but not Rs. 300: Rs. 10; (ii) for every Rs. 100 or part thereof, exceeding Rs. 300, upto Rs. 1,000: Rs. 4; (iii) for every Rs. 500, or part thereof, in excess of Rs. 1,000: Rs. 20. *Ahmedabad, Poona or other Notified City*: (i) Where it exceeds Rs. 200 but not Rs. 300: Rs. 7-8-0; (ii) for every Rs. 100 or part thereof, exceeding Rs. 300, upto Rs. 1,000: Rs. 3; (iii) for every Rs. 500, or part thereof, over Rs. 1,000: Rs. 15. *Other Bombay Urban Notified Area*: (i) Where it exceeds Rs. 200 but not Rs. 300: Rs. 4-8-0; (ii) for every Rs. 100 or part thereof, exceeding Rs. 300, upto Rs. 1,000: Rs. 1-8-0; (iii) for every Rs. 500 or part thereof, exceeding Rs. 1,000: Rs. 10.

24. COPY OR EXTRACT certified to be a true copy or extract by or by order of any public officer and not chargeable under any law for the time being in force relating to court fees (i) if the original was not chargeable with duty or if the duty with which it was chargeable does not exceed one rupee: *Eight annas*. (ii) In other cases: *One rupee*.

Exemptions: (a) Copy of any paper which a public officer is expressly required by law to make or furnish for record in any public office or for any public purpose, (b) copy of or extract from any register relating to births, baptisms, dedications, marriages, divorces, deaths or burials.

Local Acts:

(i) *Bombay, Bengal, Burma*: Re. 1. *Madras, Punjab, Bihar, C.P. & Berar*: Re. 1-8-0.

(ii) *Bombay, Bengal, Burma*: Rs. 2. *Madras, Punjab, Bihar, C.P. & Berar*: Re. 1-8-0. *U.P.*—(i) If original not chargeable with duty, or chargeable to duty not exceeding Re. 1: Annas 8 for copy or extract of agricultural lease or sale or mortgage of agricultural land; in other cases: Annas 12. (ii) In other cases, not falling under sec. 6A: Re. 1 for copy or extract of agricultural lease or sale or mortgage of agricultural lands, where original value does not exceed Rs. 1,000; in other cases: Re. 1-8-0.

25. COUNTERPART OR DUPLICATE of any instrument chargeable with duty and in respect of which the proper duty has been paid (a) if the duty with which the original instrument was chargeable does not exceed one rupee: *The same duty as is payable on the original*; (b) in other cases: *One rupee*.

Exemption: Counterpart of any lease granted to a cultivator where such lease is exempted from duty.

Local Acts: *Madras, Punjab, Bihar, C.P. & Berar, U.P.*: (i) If original duty does not exceed Re. 1-8-0: Same duty as on original. (ii) In other cases: Re. 1-8-0. *Bombay*: (i) If original duty does not exceed Rs. 2: same duty as on original; (ii) in other cases: Rs. 2. *Burma*: Rs. 2. *Bengal*: (i) If original duty does not exceed Rs. 2: Same duty as on original; (ii) in other cases, not falling within sec. 6A: Rs. 2.

27. DEBENTURE (whether a mortgage-debenture or not), being a marketable security transferable:—

(a) by endorsement, or by a separate instrument of transfer: *The same duty as a Bond (No. 15) for the same amount*.

(b) by delivery: *The same duty as a Conveyance (No. 23) for a consideration equal to the face amount of the debenture*.

Explanation:—The term 'Debenture' includes any interest coupons attached thereto, but the amount of such coupons shall not be included in estimating the duty.

Exemption: A debenture issued by an incorporated Company or other body corporate in terms of a registered mortgage-deed duly stamped in respect of the full amount of debentures to be issued thereunder, whereby the Company or body borrowing makes over, in whole or in part, their property to trustees for the benefit of the debenture holders: provided that the debentures so issued are expressed to be issued in terms of the said mortgage-deed.

Local Acts: (a) *Bengal, Madras, Punjab:* Same duty as Bottomry-Bond for such amount. (b) *Bombay City, Ahmedabad, Poona and other Notified Cities or Urban Areas:* Same duty as was leviable on a conveyance before passing of Bombay Finance Act, 1932, for consideration equal to face amount of debenture. *U.P.:* Where face amount does not exceed Rs. 100: Re. 1-4-0; where it exceeds Rs. 100 but not Rs. 200: Rs. 2-8-0; where it exceeds Rs. 200: same duty as a conveyance for face amount of debenture.

8. **DELIVERY ORDER IN RESPECT OF GOODS**, that is to say, any instrument entitling any person therein named, or his assigns, or the holder thereof, to the delivery of any goods lying in any dock or port, or in any warehouse in which goods are stored or deposited on rent or hire, or upon any wharf, such instrument being signed by or on behalf of the owner of such goods, upon the sale or transfer of the property therein, when such goods exceed in value twenty rupees: *One anna.*

DEPOSIT OF TITLE DEEDS:—See “Agreement relating to Deposit of Title-deeds, Pawn, or Pledge” (No. 6).

DISSOLUTION OF PARTNERSHIP:—See “Partnership” (No. 46).

32. **FURTHER CHARGE:**—Instrument of, that is to say, any instrument imposing a further charge on mortgaged property:—

(a) when the original mortgage is one of the description referred to in clause (a) of article No. 40 (that is, with possession): *The same duty as a Conveyance (No. 23) for a consideration equal to the amount of the further charge secured by such instrument;*

(b) when such mortgage is one of the description referred to in clause (b) of article No. 40 (that is, without possession) (i) if, at the time of execution of the instrument of further charge, possession of the property is given, or agreed to be given, under such instrument: *The same duty as a Conveyance (No. 23) for a consideration equal to the total amount of the charge (including the original mortgage and any further charge already made) less the duty already paid on such original mortgage and further charge;* (ii) if possession is not so given: *The same duty as a Bond (No. 15) for the amount of the further charge secured by such instrument.*

Local Acts: (a) *Bombay City, Ahmedabad, Poona and other Notified City or Urban Area:* Same duty as a conveyance under Bombay Finance Act, 1932, as amended, for consideration equal to greatest value of property set out in the instrument. (b) (i) *Bombay City, Ahmedabad, Poona and other Notified City or Urban Area:* Same duty as leviable on a conveyance under Bombay Finance Act, 1932, as amended, for consideration equal to total amount of charge (including original mortgage and further charge, if any, less duty already paid). (ii) *Madras:* same amount as Bottomry-Bond for amount of further charge secured by such instrument. *Burma:* Same duty as bond for whole amount payable or deliverable under such lease.

HIRING AGREEMENT or agreement for service:—See “Agreement” (No. 5).

34. **INDEMNITY-BOND:** *The same duty as a Security Bond (No. 57) for the same amount.*

INSURANCE:—See “Policy of Insurance” (No. 47).

36. **LETTER OF ALLOTMENT OF SHARES** in any Company or proposed company, or in respect of any loan to be raised by any company or proposed company: *Annas two.*

37. **LETTER OF CREDIT**, that is to say, any instrument by which one person authorizes another to give credit to the person in whose favour it is drawn: *Annas two*.

LETTER OF GUARANTEE:—See "Agreement" (No. 5).

39. **MEMORANDUM OF ASSOCIATION OF A COMPANY**:—

(a) if accompanied by Articles of Association under section 37 of the Indian Companies Act, 1882: *Rupees fifteen*; (b) if not so accompanied: *Rupees forty*.

Exemption: Memorandum of any Association not formed for profit, and registered under section 26 of the Indian Companies Act, 1882.

Local Acts: (a) *Bombay, Bengal, Bihar, C.P. & Berar, Burma, Madras, Punjab, U.P.*: Rs. 30. (b) *Bombay, Bihar, Burma, C.P. & Berar, Madras, Punjab, U.P.*: Rs. 80.

Bengal: If not so accompanied, (i) where nominal share capital does not exceed Rs. 1 lakh: Rs. 80, (ii) in other cases: Rs. 130.

40. **MORTGAGE-DEED**, not being "an Agreement relating to Deposit of Title-deeds, Pawn or Pledge" (No. 6), Bottomry-Bond (No. 16), Mortgage of a Crop (No. 41), Respondentia-Bond (No. 56) or Security-Bond (No. 57): (a) when possession of the property or any part of the property comprised in such deed is given by the mortgagor or agreed to be given: *The same duty as a Conveyance* (No. 23) for a consideration equal to the amount secured by such deed;

(b) when possession is not given or agreed to be given as aforesaid: *The same duty as a Bond* (No. 15) for the amount secured by such deed. *Madras*: *The same duty as a Bottomry-Bond* (No. 16) for the amount secured by such deed.

Explanation.—A mortgagor who gives to the mortgagee a power-of-attorney to collect rents or a lease of the property mortgaged or part thereof is deemed to give possession within the meaning of this article.

(c) when a collateral or auxiliary or additional or substituted security, or by way of further assurance for the abovementioned purpose, where the principal or primary security is duly stamped; for every sum secured not exceeding Rs. 1,000: *Eight annas*; and for every Rs. 1,000 or part thereof secured in excess of Rs. 1,000: *Eight annas*.

Exemptions: (1) Instruments executed by persons taking advances under the Land Improvement Loans Act, 1883, or the Agriculturists' Loans Act, 1884, or by their sureties as security for the repayment of such advances. (2) Letters of hypothecation accompanying a bill of exchange.

Local Acts: (a) *C.P. & Berar*: (i) Where amount secured does not exceed Rs. 50: 8 annas; (ii) where amount secured exceeds Rs. 50 but not Rs. 500, 8 annas for every Rs. 50 or part thereof; (iii) where it exceeds Rs. 500, the same duty as a Conveyance (No. 23) for amount of consideration secured. *Bombay, Ahmedabad, Poona and other Notified City or Urban Area*: Same duty as on Conveyance (No. 23) under Bombay Finance Act, 1932, as amended, for amount of consideration secured.

(b) *Madras*: Same duty as Bottomry-Bond (No. 16) for amount of consideration secured. *C.P. & Berar*: (i) Where amount secured does not exceed Rs. 10, 2 annas; (ii) where it exceeds Rs. 10 but not Rs. 500, annas 4 for every Rs. 50 or part thereof; (iii) where it exceeds Rs. 500, same duty as a Bond (No. 15) for amount secured.

(c) *Madras, Punjab, Bihar, C.P. & Berar, U.P.*: (i) For every sum secured not exceeding Rs. 1,000, 12 annas; (ii) for every Rs. 1,000, or part thereof, in excess, 12 annas. *Bengal*: (i) For every sum secured not exceeding Rs. 1,000, 12 annas; (ii) for every Rs. 1,000 or part thereof in excess, One rupee. *Bombay*: (i) For every sum secured not exceeding Rs. 1,000, One rupee; (ii) for every Rs. 1,000 or part thereof in excess, One rupee.

42. **NOTARIAL ACT**, that is to say, any instrument, endorsement, note, attestation, certificate, or entry not being a Protest (No. 50) made or signed by a Notary Public in

the execution of the duties of his office, or by any other person lawfully acting as a Notary Public: *One rupee.*

Local Acts : Bombay, Bengal, Burma, Punjab, U.P. : Rs. 2.

43. **NOTE OR MEMORANDUM** sent by a Broker or Agent to his principal intimating the purchase or sale on account of such principal:—(a) of any goods exceeding in value twenty rupees: *Two annas*; (b) of any stock or marketable security exceeding in value twenty rupees: Subject to a maximum of ten rupees, *one anna for every Rs. 10,000*, or part thereof of the value of the stock or security.

Local Acts : Madras, Bihar, C.P. & Berar : Re. 1-8.

(a) *Madras, Punjab, Bihar, C.P. & Berar, U.P. : 3 annas. Burma, Bengal : 4 annas.*

(b) *Madras, Punjab, Bihar, C.P. & Berar, U.P. : Subject to a maximum of Rs. 15, two annas for every Rs. 10,000 or part thereof of value of a stock or security. Burma : Subject to a maximum of Rs. 20, two annas for every Rs. 10,000, or part thereof, of value of stock or security. Bengal : (b) Of any stock or marketable security exceeding Rs. 20 in value and not being government security, two annas for every Rs. 5,000, or part thereof, of value of stock or security. (c) Of Government Security : Subject to a maximum of Rs. 20, two annas for every Rs. 10,000, or part thereof, of value of security.*

Bombay : (a) Of any goods exceeding in value Rs. 20, four annas; (b) of any share, scrip, stock, debenture, debenture stock or other marketable security of like nature, exceeding in value Rs. 20, not being government security, two annas for every Rs. 2,500, or part thereof, of value of security at time of its purchase or sale; (bb) of government security, subject to a maximum of Rs. 20, two annas for every Rs. 10,000, or part thereof, of value of security, at time of its purchase or sale.

Exemption : Note or Memo. sent by a broker or agent to his principal, intimating the purchase or sale on account of such principal, of a government security, or a share, scrip, bond, debenture, debenture stock or other marketable security of a like nature, in or of an incorporated company or other body corporate, entry relating to which is required to be made in a clearance list in accordance with a rule of a stock exchange recognised under the Bombay Securities Contracts Control Act, 1925.

44. **NOTE OF PROTEST BY THE MASTER OF A SHIP :** *Eight annas.*

Local Acts : Bengal, Bombay, Burma, Bihar, C.P. & Berar, U.P., Madras : One rupee.

46. **PARTNERSHIP :** (A)—Instrument of Partnership: (a) where the capital of the partnership does not exceed Rs. 500: *Two rupees eight annas*; (b) in any other case: *Ten rupees.* (B)—Dissolution of Partnership: *Five rupees.*

Local Acts : (A) (a) Bengal, Bombay, Bihar, Burma, C.P. & Berar, Madras : Rs. 5; U.P. : Rs. 3-12; where capital exceeds Rs. 500 but not Rs. 2,000, Rs. 7-8. (b) Bengal, Bombay, Bihar, Burma, C.P. & Berar, Madras : Rs. 10; U.P. : Rs. 15. (B) Bengal, Bombay, Bihar, Burma, C.P. & Berar, Madras, U.P. : Rs. 10.

PAWN OR PLEDGE :—See “AGREEMENT relating to DEPOSIT of TITLE-DEEDS, PAWN or PLEDGE” (No. 6).

47. **POLICY OF INSURANCE :** (A)—Sea-Insurance (See section 7)—

(1) for or upon any voyage—(i) where the premium or consideration does not exceed the rate of two annas or one-eighth per centum of the amount insured by the policy, if drawn singly: India—*One anna.* If drawn in duplicate, for each part: India—*Half an anna*; (ii) in any other case, in respect of every full sum of one thousand five hundred rupees and also, any fractional part of one thousand five hundred rupees insured by the policy, if drawn singly: India—*One anna.* If drawn in duplicate, for each part: India—*Half an anna.*

(2) For time : (iii) in respect of every full sum of one thousand rupees and also any fractional part of one thousand rupees insured by the policy—where the insurance shall be made for any time not exceeding six months, if drawn singly : India—*Two annas*. If drawn in duplicate, for each part : India—*One anna*. Where the insurance shall be made for any time exceeding six months and not exceeding twelve months, if drawn singly : India—*Four annas*. If drawn in duplicate for each part : India—*Two annas*.

(B) Fire Insurance and other classes of Insurance not elsewhere included in this article, covering goods, merchandise, personal effects, crops and other property against loss or damage—

(1) in respect of an original policy—(i) when the sum insured does not exceed Rs. 5,000 : India—*Eight annas* ; (ii) in any other case : India—*One rupee* ; and (2) in respect of each receipt for any payment of a premium in any renewal of an original policy : India—*One-half* of the duty payable in respect of the original policy in addition to the amount, if any, chargeable under No. 53.

(C) Accident and Sickness Insurance—(a) against railway accident valid for a single journey only : India—*One anna*.

Exemption : When issued to a passenger travelling by the intermediate or the third class in any railway.

(b) In any other case—for the maximum amount which may become payable in the case of any single accident or sickness where such amount does not exceed Rs. 1,000 and also where such amount exceeds Rs. 1,000 for every Rs. 1,000 or part thereof : India—*Two annas* : Provided that, in the case of a policy of insurance against death by accident, when the annual premium does not exceed Rs. 2-8-0 per Rs. 1,000, the duty on such instrument shall be one anna for every Rs. 1,000 or part thereof, of the maximum amount which may become payable under it.

(cc) Insurance by way of indemnity against liability to pay damages on account of accidents to workmen employed by or under the insurer or against liability to pay compensation under the Workmen's Compensation Act, 1923, for every Rs. 100, or part thereof, payable as premium : India—*One anna*.

(D) Life Insurance or other Insurance not specifically provided for : except such a Re-insurance as is described in Division E of this article—(i) for every sum insured not exceeding Rs. 250, if drawn singly : *Two annas*. If drawn in duplicate, for each part : *One anna* ; (ii) for every sum insured exceeding Rs. 250 but not exceeding Rs. 500, if drawn singly : *Four annas*. If drawn in duplicate, for each part : *Two annas* ; (iii) for every sum insured exceeding Rs. 500 but not exceeding Rs. 1,000 and also for every Rs. 1,000 or part thereof in excess of Rs. 1,000, if drawn singly : *Six annas*. If drawn in duplicate, for each part : *Three annas*.

Exemption : Policies of life insurance granted by the Director-General of the Post Office of India in accordance with rules for Postal Life Insurance issued under the authority of the Central Government.

(E) Re-Insurance by an Insurance Company which has granted a Policy of the nature specified in Division A or Division B of this article with another Company by way of indemnity or guarantee against the payment on the original insurance or a certain part of the sum insured thereby : India—*One quarter* of the duty payable in respect of the original insurance, but not less than one anna or more than one rupee.

General Exemption : (a) Letter of cover or engagement to issue a policy of insurance : Provided that, unless such letter or engagement bears the stamp prescribed by this Act for such policy nothing shall be claimable thereunder, nor shall it be available for any purpose, except to compel the delivery of the policy therein mentioned.

48. POWER-OF-ATTORNEY not being a Proxy (No. 52) : (a) when executed for the sole purpose of procuring the registration of one or more documents in relation to

a single transaction, or for admitting execution of one or more such documents: *Eight annas*: (b) when required in suits or proceedings under the Presidency Small Cause Courts Act, 1882: *Eight annas*; (c) when authorizing one person or more to act in a single transaction other than the case mentioned in clause (a): *One rupee*; (d) when authorizing not more than five persons to act jointly and severally in more than one transaction or generally: *Five rupees*; (e) when authorizing more than five, but not more than ten, persons to act jointly and severally in more than one transaction, or generally: *Ten rupees*; (f) when given for consideration, and authorizing the attorney to sell any immoveable property: *The same duty as a Conveyance (No. 23) for the amount of the consideration*; (g) in any other case: *One rupee* for each person authorized. N.B.—The term “registration” includes every operation incidental to registration under the Indian Registration Act, 1908.

Explanation:—For the purpose of this article, more persons than one, when belonging to the same firm, shall be deemed to be one person.

Local Acts: (a) *Bombay, Burma, Bengal, Punjab*: Re. 1; *Bihar, C.P. & Berar, Madras, U.P.*: 12 Annas. (b) Ditto. (c) *Bihar, C.P. & Berar, Madras, U.P.*: Re. 1-8; *Bombay, Bengal, Burma, Punjab*: Rs. 2. (d) *Bihar, C.P. & Berar, Madras, U.P.*: Rs. 7-8; *Bombay, Bengal, Burma, Punjab*: Rs. 10. (e) *Bihar, C.P. & Berar, Madras, U.P.*: Rs. 15; *Bombay, Bengal, Punjab, Burma*: Rs. 20. (f) *City of Bombay, Ahmedabad, Poona and other Notified City or Urban Area*: Same duty as was leviable on a Conveyance (No. 23) before Bombay Finance Act, 1932, for the amount of the consideration. (g) *Bihar, C.P. & Berar, Madras, U.P.*: Re. 1-8, for each person authorized; *Bombay, Bengal, Burma, Punjab*: Rs. 2, for each person authorized.

49. **PROMISSORY NOTE:** (a) when payable on demand—(i) when the amount or value does not exceed Rs. 250: *One anna*; (ii) when the amount or value exceeds Rs. 250 but does not exceed Rs. 1,000: *Two annas*; (iii) in any other case: *Four annas*. (b) When payable otherwise than on demand: *The same duty as a Bill of Exchange (No. 13) for the same amount payable otherwise than on demand*.
50. **PROTEST OF BILL OR NOTE**, that is to say, any declaration in writing made by a Notary Public or other person lawfully acting as such, attesting the dishonour of a bill of exchange or promissory note: *One rupee*.

Local Acts: *Bengal, Bombay, Bihar, Burma, C.P. & Berar, Madras, U.P., Punjab*: Rs. 2.

51. **PROTEST BY THE MASTER OF A SHIP**, that is to say, any declaration of the particulars of her voyage drawn up by him with a view to the adjustment of losses or the calculation of averages and every declaration in writing made by him against the charterers or the consignees for not loading or unloading the ship, when such declaration is attested or certified by a Notary Public or other person lawfully acting as such: *India—One rupee*.

See also “Note of Protest by the Master of a Ship” (No. 44).

Local Acts: *Bengal, Bombay, Burma, Bihar, C.P. & Berar, Madras, U.P.*: Rs. 2.

52. **PROXY**, empowering any person to vote at any one election of the members of a District or Local Board, or of a body of Municipal Commissioners, or at any one meeting of (a) Members of an incorporated Company or other body corporate whose stock or funds is or are divided into shares and transferable, (b) a Local Authority, or (c) Proprietors, Members, or Contributors to the funds of any institution: *Two annas*.
53. **RECEIPT** for any money or other property, the amount or value of which exceeds twenty rupees: *One anna*.

Exemptions: Receipt—(a) endorsed on, or contained in, any instrument duly stamped, or on any instrument exempted under the proviso to sec. 3 (instruments executed on behalf of the Crown) or any cheque or bill of exchange payable on demand, acknowledging the receipt of the consideration-money therein expressed, or the receipt of any principal money, interest, or annuity, or other periodical pay-

ment thereby secured; (b) for any payment of money without consideration; (c) for any payment of rent by a cultivator on account of land assessed to Government revenue, or (in the Presidencies of Fort St. George and Bombay) of inam lands; (d) for pay or allowances by non-commissioned officers, soldiers, sailors or airmen of His Majesty's Army or His Majesty's Military, Naval or Air Forces when serving in such capacity, or by mounted police-constables; (e) given by holders of family-certificates in cases where the person, from whose pay or allowances the sum comprised in the receipt has been assigned, is a non-commissioned or petty officer (soldier, sailor or airman) of any of the said forces and serving in such capacity; (f) for pensions or allowances by persons receiving such pensions or allowances in respect of their service as such non-commissioned or petty officers (soldiers, sailors or airmen) and not serving the Crown in any other capacity; (g) given by a headman or lambardar for land-revenue or taxes collected by him; (h) given for money or securities for money deposited in the hands of any banker, to be accounted for:

Provided that the same is not expressed to be received of, or by the hands of, any other than the person to whom the same is to be accounted for: Provided also that this exemption shall not extend to a receipt or acknowledgment for any sum paid or deposited for or upon a letter of allotment of a share or in respect of a call upon any scrip or share of or any incorporated Company or other body corporate or such proposed or intended Company or body, or in respect of a debenture being a marketable security.

54. **RE-CONVEYANCE OF MORTGAGED PROPERTY:** (a) if the consideration for which the property was mortgaged does not exceed Rs. 1,000: The *same duty as a Conveyance* (No. 23) for the amount of such consideration as set forth in the Re-conveyance; (b) in any other case: *Ten rupees*.

Local Acts: (a) *Bombay:* Same duty as a Bond (No. 15) for amount of such consideration as set forth in the reconveyance.

(b) *Bengal, Bihar, C.P. & Berar, Madras, Punjab, U.P.:* Rs. 15; *Burma:* (a) and (b) repealed, subject to a maximum of Rs. 2-8, same duty as a Conveyance (No. 23) for the amount of consideration for mortgage.

55. **RELEASE** that is to say, any instrument (not being such a release as is provided for by sec. 23A) whereby a person renounces a claim upon another person or against any specified property (a) if the amount or value of the claim does not exceed Rs. 1,000: The *same duty as a Bond* (No. 15) for such amount or value as set forth in the release; (b) in other cases: *Five rupees*.

Local Acts: (a) *Madras, Punjab:* same duty as Bottomry-Bond (No. 16) for such amount or value as set forth in the release.

(b) *Bihar, Burma, C.P. & Berar, Madras, Punjab, U.P.:* Rs. 7-8-0. *Bombay, Bengal:* Rs. 10.

56. **RESPONDENTIA-BOND**, that is to say, any instrument securing a loan on the cargo laden or to be laden on board a ship and making repayment contingent on the arrival of the cargo at the port of destination: The *same duty as a Bond* (No. 15) for the amount of the loan secured.

Local Acts: *Bengal, Madras, Punjab:* Same duty as Bottomry-Bond (No. 16) for the amount of the loan secured.

SHARE CERTIFICATE: See 19.

59. **SHARE-WARRANTS** to bearer issued under the Indian Companies Act, 1882: *One and a half times the duty payable on a Conveyance* (No. 23) for a consideration equal to the nominal amount of the shares specified in the warrant.

Exemptions: Share-warrants when issued by a Company in pursuance of the Indian Companies Act, 1882, section 30, to have effect only upon payment, as compensation for that duty, to the Collector of Stamp-revenue, of—(a) one and a half per centum of the whole subscribed capital of the Company, or (b) if any Company,

which has paid the said duty or composition in full, subsequently issues an addition to its subscribed capital—"one and a half" per centum of the additional capital so issued.

Local Acts : City of Bombay, Poona, Ahmedabad or any other Notified City or Urban Area : One and a half times the duty payable on Conveyance (No. 23) before passing of Bombay Finance Act, 1932 ; for consideration equal to the nominal amount of the shares specified in the warrant. *U.P. :* Same duty as a debenture transferable by delivery (No. 27b) for a face amount equal to the nominal amount of shares, shown in the warrant.

60. **SHIPPING ORDER** for or relating to the conveyance of goods on board of any vessel : *One anna.*
62. **TRANSFER** (whether with or without consideration) (a) of shares in an incorporated company or other body corporate : *One half of the duty payable on a Conveyance (No. 23) for a consideration equal to the value of the share ;* (b) of debentures being marketable securities, whether the debenture is liable to duty or not, except debentures provided for by sec. 8 : *One half of the duty payable on a Conveyance (No. 23) for a consideration equal to the face amount of the debenture ;* (c) of any interest secured by a bond, mortgage deed or policy of insurance (i) if the duty on such bond, mortgage deed or policy does not exceed five rupees, *the duty with which such bond, mortgage deed or policy of insurance is chargeable ;* (ii) in any other case : *Five rupees ;* (d) of any property under the Administrator Generals' Act, 1874, sec. 31 : *Ten rupees ;* (e) of any trust property without consideration from one trustee to another trustee or from a trustee to a beneficiary : *Five rupees* or such smaller amount as may be chargeable under clauses (a) to (c) of this article.

Exemptions : Transfers by endorsements (a) of a bill of exchange, cheque or promissory note ; (b) of a bill of lading, delivery order, warrant for goods or other mercantile document of title to goods ; (c) of a policy of insurance ; (d) of securities of the Central Government.

Local Acts : U.P. : (a) and (b) : Where the value of the share or the face amount of the debenture does not exceed Rs. 100 : 12 Annas ; for amount exceeding Rs. 100 but not exceeding Rs. 1,000 : 12 Annas ; for every Rs. 100, or part thereof ; for every Rs. 500, or part thereof, exceeding Rs. 1,000 : Rs. 3-12-0 ; (c) (ii) Rs. 7-8-0, provided that if by any one instrument, the interest secured by several bonds, mortgage deeds or policies of insurance is transferred, the duty payable shall be the aggregate of duties payable, if each was transferred by a separate instrument. (a) *Bombay :* 12 Annas for every Rs. 100, or part thereof, of the value of the share ; (b) *Bengal :* 12 Annas for every Rs. 100, or part thereof, of the face value of the debenture ; (c) (i) *Bombay :* Limit raised to Rs. 10. (ii) *Bombay, Bengal :* Rs. 10 ; *Bihar, Burma, C.P. & Berar, Madras, Punjab :* Rs. 7-8 ; (d) *Bengal, Burma, Madras, Punjab, U.P. :* Rs. 15 ; *Bihar, C.P. & Berar :* Rs. 20. (e) *Bengal, Burma, C.P. & Berar, Bihar, Madras, U.P., Punjab :* Rs. 7-8 or such smaller amount as may be chargeable under clauses (a) to (c) of this article.

65. **WARRANT FOR GOODS**, that is to say, any instrument evidencing the title of any person therein named, or his assigns or the holder thereof, to the property in any goods lying in or upon any dock, warehouse, or wharf, such instrument being signed or certified by or on behalf of the person in whose custody such goods may be : *Four annas.*

Local Acts : Bihar, C.P. & Berar, Madras, U.P., Punjab : 6 Annas ; *Bombay, Burma, Bengal :* 8 Annas.

LIST OF "RELATIVES" UNDER THE COMPANIES ACT, 1956

[See secs. 2(41) and 61]

- | | |
|---|---------------------------------|
| (1) Wife. | (34) Father's brother. |
| (2) Mother. | (35) Father's brother's wife. |
| (3) Father. | (36) Mother's brother. |
| (4) Mother-in-law. | (37) Mother's brother's wife. |
| (5) Father-in-law. | (38) Mother's sister. |
| (6) Son. | (39) Mother's sister's husband. |
| (7) Son's wife. | (40) Father's sister. |
| (8) Daughter. | (41) Father's sister's husband. |
| (9) Daughter's husband. | (42) Wife's father's brother. |
| (10) Grand father (father's father). | (43) And his wife. |
| (11) Grand mother (father's mother). | (44) Wife's mother's brother. |
| (12) Mother's father. | (45) And his wife. |
| (13) Mother's mother. | (46) Wife's mother's sister. |
| (14) Grand-son (son's son). | (47) And her husband. |
| (15) Grand-son's wife (son's son's wife). | (48) Wife's father's sister. |
| (16) Grand-daughter (son's daughter). | (49) And her husband. |
| (17) Grand-daughter's husband. | (50) Brother's son. |
| (18) Daughter's son. | (51) And his wife. |
| (19) Daughter's son's wife. | (52) Sister's son. |
| (20) Daughter's daughter. | (53) And his wife. |
| (21) Daughter's daughter's husband. | (54) Brother's daughter. |
| (22) Wife's father's father. | (55) And her husband. |
| (23) Wife's mother's father. | (56) Sister's daughter. |
| (24) Wife's father's mother. | (57) And her husband. |
| (25) Wife's mother's mother. | (58) Wife's brother's son. |
| (26) Brother. | (59) And his wife. |
| (27) Brother's wife. | (60) Wife's brother's daughter. |
| (28) Sister. | (61) And her husband. |
| (29) Sister's husband. | (62) Wife's sister's son. |
| (30) Wife's brother. | (63) And his wife. |
| (31) Wife's brother's wife. | (64) Wife's sister's daughter. |
| (32) Wife's sister. | (65) And her husband. |
| (33) Wife's sister's husband. | |